IN THE UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF NEW YORK

EUROPEAN COMMUNITY, Plaintiff, v. RJR NABISCO, INC., *et al.*, Defendants.	00 Civ. 6617 (NGG/VVP)
DEPARTMENT OF AMAZONAS, *et al.*, Plaintiffs, v. PHILIP MORRIS COMPANIES INC., *et al.*, Defendants.	00 Civ. 2881 (NGG/VVP) 00 Civ. 3857 (NGG/VVP) 00 Civ. 4530 (NGG/VVP) (Consolidated)

DEFENDANTS' JOINT MEMORANDUM OF LAW IN SUPPORT OF MOTION TO DISMISS UNDER RULE 12(B)(6) THE COLOMBIAN AND EUROPEAN COMMUNITY COMPLAINTS FOR FAILURE TO STATE A CLAIM UPON WHICH RELIEF CAN BE GRANTED

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Defendants in Case Numbers 2881, 3857, and 4530, filed by various Departments of the Republic of Colombia (the "Colombian Action"),[1] and defendants in Case Number 6617, filed by the European Community (the "EC Action"),[2] respectfully submit this joint

[1] This memorandum of law in support of dismissal of the Colombian Action is filed on behalf of defendants Philip Morris Companies Inc., Philip Morris Incorporated, Philip Morris International Inc., Philip Morris Products Inc., Philip Morris Latin America Sales Corporation, Philip Morris Duty Free, Inc., British American Tobacco (Investments) Limited ("BATCo") and Brown & Williamson Tobacco Corporation ("B&W"). Defendants B.A.T Industries p.l.c., BATUS Tobacco Services, Inc. and British American Tobacco (South America) Limited do not join because in the event any claim remains they will move to dismiss the Second Amended Complaint in the Colombian Action for lack of personal jurisdiction. The issues discussed herein, however, are entirely applicable to the claims against them as well. By Order of this Court approving the parties' stipulation, motions to dismiss for lack of personal jurisdiction do not have to be filed unless the instant motions to dismiss are denied.

[2] This memorandum of law in support of dismissal of the EC Action is filed on behalf of defendants Philip Morris Companies Inc., Philip Morris Incorporated, Philip Morris International Inc., Philip Morris Products Inc., Philip Morris Duty Free, Inc., RJR Nabisco, Inc., R.J. Reynolds Tobacco Company, R.J. Reynolds Tobacco International, Inc., Nabisco Group Holdings Corp., RJR Nabisco Holdings Corp., and R.J. Reynolds Tobacco Holdings, Inc.

memorandum of law in support of their motions under Federal Rule of Civil Procedure 12(b)(6) to dismiss these actions in their entirety for failure to state a claim upon which relief can be granted under the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. § 1961, *et seq*. Defendants simultaneously have filed separate motions under Federal Rules of Civil Procedure 12(b)(1) and (7) to dismiss the Colombian and EC Actions for lack of subject matter jurisdiction and lack of indispensable parties.[3] If the Court grants those jurisdictional motions, it need not reach the issues presented here.

[3] In the Colombian Action, Philip Morris-related defendants, BATCo, and B&W have filed a joint motion to dismiss under Federal Rules of Civil Procedure 12(b)(1) and (b)(7) for lack of subject matter jurisdiction and lack of an indispensable party. In the EC Action, Philip Morris has filed a separate motion to dismiss under Federal Rules of Civil Procedure 12(b)(1) and (b)(7) for lack of subject matter jurisdiction and lack of indispensable parties. The RJR-related defendants have also filed a separate motion to dismiss under Federal Rules of Civil Procedure 12(b)(1) and (b)(6), but reserve the right to raise issues under Rule 12(b)(7), if necessary, at a later date.

INTRODUCTION AND SUMMARY

These consolidated actions, which are brought by foreign political entities in the guise of civil RICO complaints, seek to use the courts of the United States to assess and collect foreign import duties and excise taxes from companies that never owed those taxes and duties in the first place. The foreign governmental plaintiffs allege that three American tobacco manufacturers (and their U.S. and foreign affiliates) engaged in separate conspiracies to "facilitate" the smuggling of cigarettes by others into plaintiffs' foreign territories in violation of the civil provisions of the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. § 1961, *et seq*. The essence of the suits is that defendants had "reason to know" that their products were being smuggled by others into foreign countries, but did nothing to stop it. In short, plaintiffs claim that defendants failed to police their customers, their customers' customers, and so on.

In a matter nearly identical to the present cases, the Honorable Thomas P. McAvoy recently dismissed a civil RICO suit brought in the Northern District of New York by the Government of Canada against a United States cigarette manufacturer for taxes allegedly lost as a result of contraband cigarette smuggling into that country. *See Attorney General of Canada v. RJ Reynolds Tobacco Holdings, Inc.*, 103 F. Supp. 2d 134 (N.D.N.Y. 2000), *appeal docketed*, No. 00-7972 (2d Cir. Aug. 11, 2000) (argument scheduled for no earlier than the week of April 16, 2001). In dismissing the suit in its entirety, Judge McAvoy held that the Court lacked subject matter jurisdiction under the Revenue Rule, *id*. at 141-44, and, in any event, that Canada had failed to state a claim under RICO. *Id.* at 150-55. The same analysis mandates dismissal here.

As set forth in detail below, plaintiffs' Complaints fail to state a RICO claim. RICO section 1964(c), which creates the civil RICO remedy, provides a private cause of action to "[a]ny person injured in his business or property by reason of a violation of section 1962 of this chapter . . . ." 18 U.S.C. § 1964(c). Thus, to state a claim, a plaintiff must allege that: (1) it is a "person injured in his business or property" (2) "by reason of" (3) "a violation of section 1962." Plaintiffs' Complaints satisfy none of these elements and suffer from additional fatal defects.

First, plaintiffs' alleged injuries – lost taxes and increased law enforcement costs – are only "sovereign" in nature and do not constitute "business or property" as those terms are defined by the Supreme Court and Second Circuit. *See, e.g., Hawaii v. Standard Oil Co.*, 405 U.S. 251, 265 (1972); *Town of West Hartford v. Operation Rescue*, 915 F.2d 92, 103-04 (2d Cir. 1990); *Attorney General of Canada*, 103 F. Supp. 2d at 153-54. Such sovereign injuries are insufficient to state a claim under RICO. Further, as foreign governmental entities, plaintiffs do not fall within the class of "persons" entitled to bring civil actions under RICO.

Second, the face of each Complaint shows that plaintiffs' alleged losses were not "by reason of" defendants' challenged conduct. Under Second Circuit law, injuries that are derivative of harms directed at a third party cannot be "by reason of" a defendant's misconduct. *See Laborers Local 17 Health and Benefit Fund v. Philip Morris, Inc.*, 191 F.3d 229, 237-39 (2d Cir. 1999); *Chera v. Chera*, No. 99 Civ. 7101, 2000 WL 1375271, at *4 (E.D.N.Y. Sept. 20, 2000). Here, all of the alleged injuries are derivative of harm to third parties – the Colombian central government and EC Member States – and are therefore barred under RICO.

Third, plaintiffs fail to plead "a violation of section 1962." 18 U.S.C. § 1964(c). To state a claim under section 1962, the Departments and the EC must first allege that defendants engaged in a pattern of "racketeering activity." *See* 18 U.S.C. § 1962(a)-(d). RICO defines "racketeering activity" to include only certain listed offenses, and the Supreme Court has held that this list is "exhaustive." *Beck v. Prupis*, 529 U.S. 494, 497 (2000). Congress deliberately excluded tax evasion and smuggling offenses from the list. Accordingly, because the gravamen of plaintiffs' alleged predicate acts are claims for smuggling or tax evasion, plaintiffs fail to state a claim under RICO. Plaintiffs attempt to avoid that problem by dressing up their offenses as claims for mail and wire fraud. But courts have rejected similar attempts to circumvent RICO's statutory requirements. *See Bald Eagle Area Sch. Dist. v. Keystone Fin., Inc.*, 189 F.3d 321, 330 (3rd Cir. 1999); *Smith v. Jackson*, 84 F.3d 1213, 1217-18 (9th Cir. 1996). Moreover, even if considered under the mail and wire fraud statutes, the claims here are foreclosed by two recent Supreme Court cases interpreting those statutes. *See Cleveland v. United States*, 121 S. Ct. 365 (2000); *Neder v. United States*, 527 U.S. 1 (1999). Plaintiffs also fail to allege other specific requirements of RICO's four substantive provisions, including the types of injuries necessary to state a claim under sections 1962(a) and (b), the "operation or management" of an "enterprise" as required by section 1962(c), and a RICO conspiracy under section 1962(d).

Fourth, the predominately foreign conduct at issue here falls outside the scope of the RICO statute. As the Supreme Court has explained, "[i]t is a longstanding principle of American law 'that legislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States.'" *EEOC v. Arabian*

Am. Oil Co., 499 U.S. 244, 248 (1991) (citations omitted); *accord Smith v. United States*, 507 U.S. 197, 203-04 (1993) (quoting same). The RICO statute is silent as to its extraterritorial application and there is no evidence that Congress intended RICO to apply extraterritorially. So, as a matter of statutory construction, the statute cannot apply to the claims here.

Even if the presumption against extraterritorial application were overcome (and it is not), the Court would lack subject matter jurisdiction to hear plaintiffs' claims because none of the adverse effects of the alleged conduct was sustained in the United States and all of the activities material to the completion of the purported wrongdoing were completed abroad. *See North South Fin. Corp. v. Al-Turki*, 100 F.3d 1046, 1051 (2d Cir. 1996).

Fifth, plaintiffs seek equitable remedies unavailable under RICO. RICO consistently has been interpreted as barring equitable relief for private suits brought by plaintiffs other than the U.S. government. *See Trane Co. v. O'Connor Sec.*, 718 F.2d 26, 28-29 (2d Cir. 1983); *Bernard v. Taub*, No. 90 Civ. 0501, 1990 WL 34680, at *3 (E.D.N.Y. Mar. 21, 1990). Hence, the equitable remedies sought by plaintiffs fail to state a claim.

Finally, in addition to failing to state a claim under RICO, the Complaints here contain other dispositive pleading deficiencies. By improperly grouping defendants together and failing to specify any misconduct by each defendant, plaintiffs fail to plead fraud with particularity as required by Federal Rule of Civil Procedure 9(b), and improperly seek to hold defendants' holding companies liable for conduct allegedly committed by their subsidiary operating corporations.

Since all of plaintiffs' RICO claims must be dismissed, and there are no other grounds for federal jurisdiction, all of plaintiffs' pendent state law tort claims should be summarily dismissed as well.

BACKGROUND[4]

A. The Parties

1. The Plaintiffs in the Colombian and EC Actions

The plaintiffs in the Colombian Action, various Departments of the Republic of Colombia and Santa Fe De Bogota, Capital District (collectively the "Departments"), are political subdivisions of the Republic of Colombia. (Colom. 2d Am. Compl. ¶ 6.) Although the Republic of Colombia is a unitary state that may create or dissolve any given Department at the will of the national legislature, the Complaint alleges that the Departments are autonomous from the Colombian central government and that each "has rights and responsibilities comparable to that of a state of the United States." (*Id.*) The Departments alone – and not the Republic of Colombia – are the plaintiffs. (*Id.*)

The plaintiff in the EC Action is the European Community (the "EC"). According to its Complaint, the EC "is a governmental body created as a result of collaboration among the majority of the nations of Western Europe, more specifically, Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, Sweden, and the United Kingdom." (EC

[4] A motion to dismiss under Federal Rule of Civil Procedure 12(b)(6) requires that a defendant treat all non-conclusory allegations in a complaint as true. *See Laborers Local 17 Health and Benefit Fund v. Philip Morris, Inc.*, 191 F.3d 229, 234 (2d Cir. 1999); *Medgar Evers Houses Tenants Ass'n v. Medgar Evers Houses Assocs., L.P.*, 25 F. Supp. 2d 116, 120 (E.D.N.Y. 1998), *aff'd*, 201 F.3d 430 (2d Cir. 1999). Accordingly, although defendants vigorously dispute and are prepared, if required, to disprove the allegations in the Colombian and EC Complaints, for purposes of this Rule 12(b)(6) motion only, the allegations will be accepted as true.

Compl. ¶ 6.) Although not a single one of the EC's member countries (the "Member States") is a plaintiff in the EC Action – and although the EC has no authority to file suit in the United States on its own behalf or on behalf of any Member State – the EC purports to be acting "on behalf of the Member States it has power to represent." (EC Compl. p. 1.)

2. The Defendants in the Colombian and EC Actions

The defendants in the Colombian Action are entities affiliated with United States and foreign tobacco companies. The Complaint places defendants into two groups and alleges a separate and distinct conspiracy by each group. The first group includes entities affiliated with Philip Morris Incorporated. These defendants are referred to collectively in the Complaint as the "Philip Morris Defendants" or "Philip Morris." (Colom. 2d Am. Compl. ¶¶ 7-15.)[5] The second group includes entities affiliated with B.A.T Industries p.l.c. These defendants are referred to collectively in the Complaint as "the BAT Defendants." (Colom. 2d Am. Compl. ¶¶ 16-25.)

Modeled after the Colombian Action, the EC Complaint also places defendants into two groups and alleges a separate and distinct conspiracy by each group. Again, one of the groups includes entities affiliated with Philip Morris. (EC Compl. ¶¶ 16-20.) Unlike the Colombian Action, however, the second group does not include any of the BAT Defendants. Rather, the second group in the EC Action consists of entities

[5] As discussed in Part VI below, plaintiffs improperly group all of the defendants by corporate affiliation. Each defendant, however, is a separate and independent entity, some of which are mere holding companies, not engaged in the manufacture, sale, or marketing of cigarettes. For convenience, we will refer to each group of defendants collectively as alleged in the Complaints.

affiliated with R.J. Reynolds Tobacco Company that are referred to collectively as the "RJR Defendants." (EC Compl. ¶¶ 7-15.)

B. The Alleged Smuggling Schemes in the Colombian and EC Actions

Although the Colombian and EC Actions span different continents, involve different groups of defendants, and different distributors, the allegations in the two actions are substantially similar, and many of the allegations in the EC Complaint appear to have been lifted virtually verbatim from the Colombian Complaint. Accordingly, the relevant allegations against all of the defendants in the Colombian and EC Actions will be discussed jointly, with any material difference noted.

The four separate conspiracies in the Colombian and EC Actions are alleged to have worked in the same general way: The defendants (lawfully) sold cigarettes to various unnamed foreign cigarette distributors. (Colom. 2d Am. Compl. ¶¶ 37(a) to (ww) (PM); 38(a) to (ddd) (BAT Defendants); EC Compl. ¶¶ 32 (RJR); 33-34 (PM).) Those distributors, in turn, sold the cigarettes to various unnamed "smugglers," who, in turn, illicitly transported the cigarettes into Colombia or various EC Member States or sold to those that did. (*Id.*) The smugglers then purportedly bypassed government customs officials and evaded paying taxes on the "contraband" cigarettes. (Colom. 2d Am. Compl. ¶¶ 45-46; EC Compl. ¶¶ 39-40.)

Notably, the Colombian and EC Complaints do not allege that defendants' sales of cigarettes to their distributors – or to any alleged "smuggler" – were themselves unlawful. Indeed, those sales were completely legal. Nor do the Complaints allege that defendants themselves smuggled goods into Colombia or any EC Member State or failed

to pay taxes due at the time of import.[6] Rather, the Complaints allege that defendants "controlled, directed, encouraged, supported, and facilitated the activities of [unnamed third party] smugglers." (Colom. 2d Am. Compl. ¶ 29; EC Compl. ¶ 24.)

First, the Complaints allege that defendants "supported" smuggling by simply *selling their products.* The essence of this charge is that defendants should have better policed their customers (and those who purchased from their customers), but instead purportedly sold cigarettes to unidentified entities (who are not parties in this case) whom they "had reason to know" were involved in smuggling. (Colom. 2d Am. Compl. ¶¶ 32(a), (b); 33; 37(h)-(k), (r)-(t), (bb)-(hh) (PM); 38(a), (g), (u), (v), (aa) (BAT Defendants); EC Compl. ¶¶ 27(a), (b); 28; 32(c), (e)-(n), (t) (RJR); 33(a), (f)-(k), (m)-(n), (u) (PM).)

Second, the Complaints allege that defendants "encourage[d]" smuggling by *marketing lawfully imported products.* For example, the Colombian Complaint alleges that defendants used their lawful cigarette imports and sales in Colombia as an "umbrella operation" to help foster and conceal the market for contraband cigarettes smuggled into the country by third parties. (Colom. 2d Am. Compl. ¶¶ 37(d), (g) (PM); 38(m) (BAT Defendants).) The EC Complaint charges that defendants provided marketing information to their distributors in conjunction with lawfully imported products and that

[6] In the Colombian Action, the Departments allege that defendants "under-invoiced" lawful imports reducing the amount of import duties allegedly owed to the non-party Colombian central government. As discussed below, however, the Departments do not seek damages for lost import duties because those funds are imposed for the exclusive benefit of the Colombian central government. Also, there is litigation pending in Colombia regarding the underinvoicing matter.

those distributors, in turn, used that marketing data to promote the sale of contraband products. (EC Compl. ¶ 27(d).)

Third, the Complaints allege that defendants "facilitated" smuggling through their *standard business practices* and by *denying their involvement in smuggling*. Specifically, the Complaints allege that defendants' cigarette distribution chains and payment processes "make it more difficult for investigators to distinguish between legitimately and illegitimately sold cigarettes and . . . make it difficult or impossible for legal authorities to track the payment for the cigarettes and the ultimate destination of the cigarettes." (Colom. 2d Am. Compl. ¶¶ 37(m) (PM); 38(cc)-(dd) (BAT Defendants); EC Compl. ¶ 32 (p)-(s) (RJR); 33(l) (PM).) The Complaints further assert that defendants' cigarette packaging labels and shipping papers – which are not alleged to be non-conforming with applicable laws – nevertheless make it "more difficult" for customs officials to detect smuggling. (Colom. 2d Am. Compl. ¶¶ 32(c), (e); 37(x) (PM); 38(dd) (BAT Defendants); EC Compl. ¶¶ 32(c), (r) (RJR); 27(c), (e) (PM).) Additionally, the Complaints contend that defendants "falsely represented to the law-enforcement agencies of various governments . . . that they were attempting to combat smuggling when, in fact, they were actively supporting smuggling." (Colom. 2d Am. Compl. ¶¶ 37(w) (PM); 38 (bb) (BAT Defendants); EC Compl. ¶¶ 32(p) (RJR); 33(p) (PM).) Defendants also somehow facilitated smuggling by allegedly "falsely stat[ing] that smuggling is caused by high taxes." (Colom. Compl. ¶¶ 37(uu) (PM); 38(aaa) (BAT Defendants); EC Compl. ¶¶ 33(p) (RJR); 34(l) (PM).)

Finally, the Colombian Complaint alleges that Philip Morris and the BAT Defendants "directed and controlled" smuggling by purportedly engaging in a

"systematic process of 'underinvoicing' their otherwise legitimately imported cigarettes into Colombia" as a way of avoiding import duties. (Colom. 2d Am. Compl. ¶¶ 37(e) (PM); 38(c) (BAT Defendants).) Because import duties belong only to the Republic of Colombia, however, the Departments claim no damage as a result of lost import duties. Instead, they allege that "underinvoicing" in some way facilitates smuggling by "fixing" the price of contraband cigarettes. (Colom. 2d Am. Compl. ¶¶ 30(b), 37(f), (ff), (gg), (nn) (PM); 38(d), (q)-(s) (BAT Defendants).)

C. The Departments' and EC's Alleged Injuries – Lost Taxes and Duties and Increased Law Enforcement Costs

1. The Colombian Action Alleges That Defendants Interfered With the Collection of Taxes Owed to the Central Government

The Departments claim that the alleged smuggling operation caused them "hundreds of millions of dollars" in damages as the result of defendants' alleged interference with their ability to collect taxes from third parties. (Colom. 2d Am. Compl. ¶ 46.)[7] Principally, these alleged damages take the form of lost tax revenue[8] the

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[7] The Colombian Complaint alleges as follows:

> As a result of the activities of the Defendants, large amounts of cigarettes are smuggled into the Departments of the Republic of Colombia and the proper taxes are not paid on the aforesaid cigarettes. As a result of the Defendants' wrongful activities, the Plaintiffs, the Departments of the Republic of Colombia, have been deprived of the money and property that they would have obtained from the lawful importation and sale of cigarettes . . . .

(Colom. 2d Am. Compl. ¶ 45.)

[8] In prior complaints, the Colombian Departments also sought damages for allegedly lost import duties. After proceedings regarding Philip Morris' Motion to Stay revealed that only the Colombian central government, and not its Departments, impose or receive the benefits from import duties, the Departments amended their Complaint, abandoning their claims for reimbursement of these import duties. (*Compare* Colom. 2d Am. Compl. ¶ 4 *with* original Colom. Compl. ¶ 4.) The Departments, however, continue to rely on allegations that Philip Morris and the BAT Defendants misstated the value of their products in declarations relating to import duties in support of their claims. (*See* Colom. 2d Am. Compl. ¶¶ 30(b), 37(f), (j), (cc), (ff), (gg), (nn).)

Departments claim they would have received from importers had contraband cigarettes entered Colombia in a lawful manner. (Colom. 2d Am. Compl. ¶ 45.)

It is important to understand two points regarding the Departments' alleged tax losses. *First*, under Colombian law only the (non-party) Republic of Colombia, not the Departments, has power to levy the taxes in question. The Departments' losses, if any, are merely as a beneficiary of those national taxes, which are deposited into a national account fund for ultimate distribution to the Departments. (*See* discussion *infra* Part III.A.)

Second, the Colombian Complaint nowhere alleges that any defendant itself failed to declare or pay taxes due or otherwise owes taxes on any contraband cigarettes. Rather, the Complaint alleges that unnamed third party smugglers – who evaded the authorities and would have been liable for the taxes had the cigarettes been imported lawfully – failed to declare and pay the applicable taxes at the time of entry. The Complaint alleges only that defendants *interfered* with tax collection by purportedly engaging in conduct that made it "more difficult" for Colombian tax officials to detect smuggling and collect taxes from third party smugglers. (Colom. 2d Am. Compl. ¶¶ 32(f)-(h); 37(a)-(b), (j), (l), (n), (t), (v) (PM); 38(b)-(c), (p), (q), (v)-(y), (aa)-(bb), (dd), (hh), (ll), (qq) (BAT Defendants).)

In addition to these alleged tax losses, the Colombian Action claims that defendants are liable for increased law enforcement costs that the Departments were forced to incur "in their efforts to stop smuggling and to recoup funds that they have lost as a result of the activities of the Defendants." (Colom. 2d Am. Compl. ¶ 46.)

2. The EC Action Alleges That Defendants Injured the EC By Depriving the (Non-Party) Member States of Taxes and Duties That Are Used by the Member States to Fund the EC's Budget

The EC claims that the alleged smuggling operation resulted in "billions of dollars" in damages. (EC Compl. ¶¶ 4, 40.) Principally, these alleged damages take the form of lost customs duties and value-added taxes ("VAT") that the EC claims would have been collected by Member States and later used by the Member States to fund the EC's budget had the contraband cigarettes entered the Member States in a lawful manner. (EC Compl. ¶ 39.)[9]

As with the Colombian Action, it is important to understand two points regarding these alleged European customs duty and VAT losses. *First*, the EC's budget is funded in part through taxes and duties collected from imports into Member States. However, EC law requires that Member States cover any shortfall in the anticipated EC budget resulting from losses in duties and VAT and to pay that shortfall from other sources of revenue. By law, then, the EC's budget is protected from shortfalls caused by the failure of Member States to collect or receive duties and VAT from importers. (*See* discussion *infra* Part I.B.)

Second, the EC Action does not allege that any defendant itself failed to declare or pay duties or VAT on contraband cigarettes. Like the Colombian Complaint, the EC

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[9] The EC Complaint alleges as follows:

> As a result of the Defendants' wrongful activities, the Plaintiff, the European Community, including its Member States, have been deprived of the money and property that they would have obtained from the lawful importation and sale of cigarettes. This money and property includes, but is not limited to the following: (a) Customs duties that are levied exclusively for the benefit of the European Community; and (b) Value-added tax levied on cigarettes.

(EC Compl. ¶ 39.)

Complaint claims only that the duties and VAT were not paid by unidentified third party smugglers and that defendants interfered with the Member States' ability to collect duties and taxes from those smugglers.

In addition, the EC, like the Departments, claims that defendants are liable for increased law enforcement costs that the EC purportedly was forced to incur "in its efforts to stop smuggling and to recoup funds that it has lost as a result of the activities of the Defendants." (EC Compl. ¶ 40.)

ARGUMENT

I. THE COLOMBIAN AND EC COMPLAINTS FAIL TO ALLEGE THAT A "PERSON" HAS BEEN "INJURED IN HIS BUSINESS OR PROPERTY"

RICO section 1964(c), which creates the civil RICO remedy, provides a private cause of action to "[a]ny person injured in his business or property . . . ." 18 U.S.C. § 1964(c).[10] The Departments and EC fail to meet those threshold pleading requirements because they claim only sovereign injuries that do not constitute "business or property" as those terms are defined by the Supreme Court and Second Circuit. Further, because the EC in fact could suffer no out-of-pocket financial loss from alleged smuggling into its Member States, the EC fails to allege that it even has been "injured." Finally, as foreign governmental bodies, the Departments and EC are not "persons" within the meaning of RICO.

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[10] RICO section 1964(c) provides:

> Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therefor in any appropriate United States district court and shall recover threefold the damages he sustains and the cost of the suit, including a reasonable attorney's fee.

18 U.S.C. § 1964(c).

A. The Departments and EC Fail to Plead Any Injury to "Business or Property"

The Court should dismiss the Colombian and EC Complaints because they fail to plead injury to "business or property." The law is clear that under RICO section 1964(c), injury to "business or property" means only "commercial" injury suffered as a market participant, not "sovereign" injury. *See Hawaii v. Standard Oil Co.*, 405 U.S. 251, 262-65 (1972); *Town of West Hartford v. Operation Rescue*, 915 F.2d 92, 103-04 (2d Cir. 1990). Hence, when a governmental body claims injury to its general economy or injury stemming from carrying out its official functions or police powers – such as lost taxes or increased law enforcement costs – courts repeatedly have held that such losses do not constitute injury to "business or property" under RICO or the antitrust laws upon which RICO's treble-damages provision was modeled. *See Hawaii*, 405 U.S. at 262-64; *Town of West Hartford*, 915 F.2d at 103-04; *Attorney General of Canada*, 103 F. Supp. 2d at 152-55; *accord Dillon v. Combs*, 895 F.2d 1175, 1177 (7th Cir. 1990); *Town of Brookline v. Operation Rescue*, 762 F. Supp. 1521, 1522-23 (D. Mass. 1991).

In the leading Second Circuit case, for example, a town in Connecticut allegedly incurred substantial law enforcement expenses responding to a large-scale political protest. *See Town of West Hartford*, 915 F.2d at 98-99. The town sought to recover those expenses by bringing a RICO suit against the activists who participated in the protest. *See id*. Relying on the Supreme Court's interpretation of "business or property" under the Clayton Act (upon which RICO's private right of action was based), the Second Circuit determined that the town's increased law enforcement costs were not cognizable injuries under RICO. *See id.* at 103-04. The court reasoned that such injuries were not suffered by the town in its capacity as a consumer of goods and services, but were

economic injuries to its sovereign interests of the sort that "do not fall within the ambit of section 1964(c)." *Id*. at 104.

Applying this well-settled rule, the court in *Attorney General of Canada v. RJ Reynolds Tobacco Holdings, Inc.*, dismissed RICO claims similar to those made here. There, Canada brought a RICO action against a cigarette manufacturer claiming that the manufacturer conspired to smuggle cigarettes into that country. *See Attorney General of Canada*, 103 F. Supp. 2d at 137-38. In addition to claiming damages for lost tax revenue from the smuggling, Canada sought recovery for law enforcement expenses it incurred "to stop the smuggling and catch the wrongdoers." *Id*. at 143. After dismissing the claim for lost taxes under the Revenue Rule, the court determined that the Second Circuit's decision in *Town of West Hartford* mandated dismissal of the claim for increased law enforcement costs as well:

> [T]he holding in *Town of West Hartford* compels the Court to conclude that such costs do not constitute a cognizable RICO injury to Canada as a party to a commercial transaction, but, rather, constitute injury to Canada's general economy and its ability to carry out its functions. Because the cost of law enforcement pertains to general municipal functions rather than commercial activities, under *Town of West Hartford*, Canada may not recover for such damages under RICO.

Id. at 155.

Other decisions are in accord, including some that have applied this reasoning in the context of governmental efforts to collect unpaid taxes. In *Michigan v. Fawaz*, 653 F. Supp. 141, 143 (E.D. Mich. 1986), *aff'd*, 848 F.2d 194 (table), 1988 WL 44736 (6th Cir. May 9, 1988), for example, the district court and the Sixth Circuit both dismissed a State's claim for treble damages under RICO stemming from a scheme to defraud the

state of taxes. And *West Virginia v. Moore*, 895 F. Supp. 864, 872 (S.D. W. Va. 1995), did the same, holding that RICO could not be used to recoup unpaid taxes. For like reasons, this Circuit and others have refused to recognize RICO claims brought by government entities on behalf of their citizens. *See Abrams v. Seneci*, 817 F.2d 1015, 1017-18 (2d Cir. 1987) (concluding that New York could not bring RICO treble-damages action in capacity to recover citizens' losses from the marketing of fraudulent video games, vending machines and automobile batteries); *Dillon*, 895 F.2d at 1177 (sovereign interests are not "business or property" and a "State has its own laws and ample access to its own courts, through which it may protect its residents from fraud.").

1. Lost Taxes and Duties Are Sovereign – Not Commercial – Injuries

Both the Departments and the EC allege that they have been "injured in their business and property" as a result of defendants' conduct. (Colom. 2d Am. Compl. ¶¶ 55, 64, 73, 80; EC Compl. ¶¶ 49, 53, 58, 67, 123, 132, 141.) Their primary alleged losses, however, are for lost excise taxes supposedly owed to the Departments by unnamed third parties (Colom. 2d Am. Compl. ¶¶ 45-46), and lost customs duties and VAT supposedly owed to the EC's Member States by others. (EC Compl. ¶¶ 39-40.) Yet, it is indisputable that the imposition and collection of taxes are quintessentially "sovereign" activities. *See Wyoming v. Oklahoma*, 502 U.S. 437, 451 (1992) (a state's effort to recover lost tax revenue is "beyond peradventure . . . an action undertaken in its sovereign capacity."); *Merrion v. Jicarilla Apache Tribe*, 455 U.S. 130, 146 (1982) (Indian tribe acts as a sovereign when it imposes taxes on economic activities within its jurisdiction).

As such, the losses at issue here – whether incurred by the Departments, the EC, or the non-party Member States – are not commercial injuries, but sovereign injuries not cognizable under RICO.

2. Expenses Incurred For Law Enforcement Are Sovereign – Not Commercial – Injuries

As for the Departments' and EC's alleged damages for increased law enforcement expenditures, the *Hawaii*, *Town of West Hartford*, and *Attorney General of Canada* decisions squarely hold that these are sovereign in nature and cannot support a claim under RICO. *See Hawaii*, 405 U.S. at 262-65; *Town of West Hartford*, 915 F.2d at 103-04; *Attorney General of Canada*, 103 F. Supp. 2d at 155.

* * *

In the end, plaintiffs' attempt to recover for taxes, duties, and law enforcement costs does not stem from their decision to become "a party to a commercial transaction," but instead constitutes precisely the kind of "sovereign" injuries that the Supreme Court and Second Circuit preclude. Such recoveries simply are not allowed. The purpose of establishing a RICO treble-damages remedy was to encourage those directly injured by anti-competitive conduct to act as "private attorneys general," not to allow government surrogates to do so in their place and least of all to allow foreign government claimants to do so in the context of such eminently sovereign injuries.

B. The EC Fails to Plead That it Has Been "Injured" At All Because It Suffers No Financial Loss From the Failure of Smugglers to Pay Duties and VAT to Member States

In addition to the disqualifying sovereign nature of plaintiffs' alleged injuries, there is an independent reason to dismiss the EC's RICO claims: the EC has not been

"injured" from the alleged smuggling conspiracies. RICO section 1964(c) "requires a showing of some actual, out-of-pocket financial loss." *Dornberger v. Metropolitan Life Ins. Co.*, 961 F. Supp. 506, 521 (S.D.N.Y. 1997); *accord Maio v. Aetna, Inc.*, 221 F.3d 472, 483-84 (3rd Cir. 2000) (summarizing cases and concluding that "the injury to business or property element of section 1964(c) can be satisfied by allegations and proof of actual monetary loss, i.e., an out-of-pocket loss"); *Berg v. First State Ins. Co.*, 915 F.2d 460, 464 (9th Cir. 1990) ("[A]bsent damages, a RICO claim cannot be sustained."). Here, as a matter of law, the EC has suffered no monetary loss from any alleged failure of its Member States to collect duties and VAT on smuggled products.

Under EC law, the EC's budget is funded through certain designated sources of revenue (called "own resources") collected by the Member States. *See, e.g.*, Council Decision 94/728, of 31 October 1994, on the System of the European Communities' Own Resources, art. 2, 1994 O.J. (L 293) 10.[11] Those sources of revenue include customs duties and VAT collected on products imported into Member States. *Id*. Failure of the Member States to collect duties and VAT on imported products, however, does not relieve them of their obligation to the EC. Rather, EC law mandates that the Member States fund the EC budget *in full*, even if duties and VAT on imported products are not collected. *See* Council Regulation 1150/2000, of 22 May 2000, Implementing Decision 94/728/EC, Euratom on the System of the European Communities' Own Resources, arts. 5, 17, 2000 O.J. (L 130) 3, 8. Consequently, the EC could not suffer any loss from

[11] Pursuant to Federal Rule of Civil Procedure 44.1, this Court "may consider any relevant material or source," including foreign statutes and cases to determine foreign law. That determination is treated as "a question of law." Fed. R. Civ. P. 44.1; *accord Carlisle Ventures, Inc. v. Banco Espanol de Credito, S.A.*, 176 F.3d 601, 604 (2d Cir. 1999).

smuggling or other conduct that might reduce duties and VAT collected by Member States. Accordingly, even if Member States did fail to collect duties and VAT on smuggled cigarettes, the EC would not be "injured," much less injured in its "business or property."

C. As Government Bodies, the Departments and EC Are Not "Persons" Entitled to Bring Civil RICO Actions

Only a "person" may bring a civil RICO action. 18 U.S.C. § 1964(c) ("Any *person* injured in his business or property . . . may sue.") (emphasis added). Here, the Complaints fail to state a claim because neither the Departments nor the EC is a "person" for purposes of RICO.

1. The Clear Statement Rule Excludes Foreign Governments from the Definition of a RICO "Person"

Under the "clear statement rule," a government body is not a "person" under a federal statute unless Congress has made it unmistakably clear in the statutory language or legislative history that it intended to include governments within the scope of the statute. *See Will v. Michigan Dep't of State Police*, 491 U.S. 58, 65 (1989). In accordance with this rule, the Second Circuit has held that the United States is not a "person" under RICO. *See United States v. Bonanno Organized Crime Family of La Cosa Nostra*, 879 F.2d 20, 21-26 (2d Cir. 1989).[12] Similarly, the Supreme Court recently

[12] The analysis in *Bonanno* has been followed both within and without the Second Circuit in decisions holding that federal, state, and tribal governments are not persons subject to suit. *See, e.g.*, *United States v. Private Sanitation Indus. Ass'n of Nassau/Suffolk, Inc.*, 793 F. Supp. 1114, 1149 (E.D.N.Y. 1992) (government was not a "person" under RICO); *Bair v. Krug*, 853 F.2d 672, 674-75 (9th Cir. 1988) (Nevada was immune from RICO suit); *McMaster v. Minnesota*, 819 F. Supp. 1429, 1434-35 (D. Minn. 1993) (Minnesota was immune from RICO suit), *aff'd*, 30 F.3d 976 (8th Cir. 1994); *Andrade v. Chojnacki*, 934 F. Supp. 817, 831 (S.D. Tex. 1996) (United States may not be a RICO civil defendant); *Smith v. Babbitt*, 875 F. Supp. 1353, 1365 (D. Minn. 1995) ("Absent a congressional or tribal waiver, the [Indian tribe], like other sovereigns, is immune from suit for alleged RICO violations.").

ruled that states of the United States are not "persons" under the False Claims Act ("FCA"), 31 U.S.C. § 3729 *et seq.*, because the unequivocal intent to include them is not evident in the FCA's statutory language or legislative history. *See Vermont Agency of Natural Res. v. Stevens*, 529 U.S. 1858 (2000).

The exclusion of governments from the definition of "person" is particularly important when their inclusion could impinge on foreign sovereignty. Foreign sovereign immunity is, of course, based on long standing principles of common law and international law and was well established when Congress enacted RICO in 1970.[13] *See Alfred Dunhill of London, Inc. v. Republic of Cuba*, 425 U.S. 682, 698-06 (1976); *Victory Transp. Inc. v. Comisaria General de Abastecimientos y Transportes*, 336 F.2d 354, 357-59 (2d Cir. 1964). "In traditionally sensitive areas . . . the requirement of clear statement assures that the legislature has in fact faced, and intended to bring into issue, the critical matters involved in the judicial decision." *Will*, 491 U.S. at 65 (citations omitted). Since Justice Marshall's decision in *The Schooner Exchange v. McFadden*, 11 U.S. 116 (1812), it has been recognized that the United States will not be deemed to have exercised its power to deny foreign sovereign immunity from suit "until such power be exerted in a manner not to be misunderstood." *Id.* at 146; *accord Environmental Def. Fund, Inc. v. Massey*, 986 F.2d 528, 531 (D.C. Cir. 1993) ("The Supreme Court [has] refused, in the absence of a clear statement of extraterritorial scope, to infer congressional intent to apply the federal statute to the conduct of a foreign government because enforcement

[13] Common law principles of foreign sovereign immunity, which immunize the non-commercial activities of foreign governments, were codified in 1976 in the Foreign Sovereign Immunities Act. *See* 28 U.S.C. § 1602 *et seq.; see also* 1 Restatement (Third) of the Law, Foreign Relations of the United States, § 451 (1987).

would have interfered with the exercise of foreign sovereignty"); *see also Benz v. Compania Naviera Hidalgo, S.A.*, 353 U.S. 138, 147 (1957) ("For us to run interference in such a delicate field of international relations there must be present the affirmative intention of the Congress clearly expressed.").

In the RICO context, application of the clear statement rule requires a finding that "person" does not include foreign sovereigns. RICO originally was drafted as a criminal statute "to seek the eradication of organized crime" through criminal prohibitions and limited civil injunctive remedies that could be pursued only by the United States. *Statement of Findings and Purpose,* Pub. L. No. 91-452, 84 Stat. 922, 923 (1970), *reprinted in* 1970 U.S.C.C.A.N. 1073; *see also* S. 30, 91st Cong., 1st Sess. (1969) (original bill). Thus, the term "person" as used in the original bill was intended to encompass individuals and business entities that could be criminally charged, prosecuted, and jailed or fined. Late in the legislative process, a private civil remedy was added to the bill, allowing persons to sue (or be sued) for treble damages. *See* H.R. 1549, 91st Cong., 2d Sess. (1970). "The object of civil RICO is thus not merely to compensate victims but to turn them into prosecutors, 'private attorneys general[.]'" *Rotella v. Wood*, 528 U.S. 549, 557 (2000).

RICO uses the same term – "person" – in its criminal prohibitions and to identify both those who may sue and those who may be sued under the statute. *Compare* 18 U.S.C. § 1962 ("It shall be unlawful for any *person* . . . .") *with* § 1964(c) ("Any *person* injured in his business or property . . . may sue") *with* § 1965(a) (allowing "civil action . . . against any *person*") (emphasis added). RICO employs a single definition of "person." *See* 18 U.S.C. § 1961(3). "[T]he statute does not distinguish between the

definition of a potential plaintiff and defendant." *Bonanno*, 879 F.2d at 22-23; *cf. United States v. Cooper Corp.*, 312 U.S. 600, 606 (1941) (giving consistent interpretation to "person" in Sherman Act, reasoning "[i]t is hardly credible that Congress used the term 'person' in different senses in the same sentence."). Thus, if a foreign government were a "person" who could sue, it also would be a "person" who could be sued civilly under RICO and a "person" who could be prosecuted criminally. But the statute evinces no intent, much less a clear intent, to abrogate foreign sovereign immunity, particularly in the criminal context. Absent an unequivocal expression of congressional intent that foreign governments could be haled into court under RICO, no such abrogation should occur. Accordingly, foreign governments cannot be either RICO plaintiffs or RICO defendants.[14]

Expansion of the definition of "person" to include government bodies would make little sense. First, it would require the absurd result that foreign sovereigns could be prosecuted criminally. *See* 1 Restatement (Third) of Foreign Relations Law § 451 & cmt. a (foreign states immune from jurisdiction of courts, except for commercial activities); § 461 cmt. d ("A state itself is generally not subject to the criminal process of another state"); and § 464 (absolute immunity from criminal process for diplomats). Second, it would expand the purpose of the civil provisions beyond creating private

[14] While a few non-binding decisions have indicated that foreign sovereigns may constitute "persons" under the antitrust laws or RICO, none of those decisions applied the clear statement rule and all are inconsistent with the Second Circuit's decision in *Bonanno*. *See Pfizer, Inc. v. Government of India*, 434 U.S. 308, 320 (1978) (foreign government "person" under antitrust laws); *Republic of the Philippines v. Marcos*, 862 F.2d 1355, 1358 (9th Cir. 1988) (foreign government "person" under RICO); *Attorney General of Canada*, 103 F. Supp. 2d at 150 (same). Measured against the strict requirements of the clear statement rule, however, the EC and Departments plainly fall outside the definition of a "person" who may sue or be sued under RICO's civil-remedy provision.

attorneys general to creating financial incentives for foreign governments to sue in U.S. courts. Section 1964(c) not only creates a treble-damages civil remedy, but also provides for an award of "the cost of the suit, including a reasonable attorney's fee." 18 U.S.C. § 1964(c). Few, if any, statutes authorizing lawsuits by governments contain such a provision. *See Cooper Corp.*, 312 U.S. at 606. Governments need no moral incentive to vindicate public rights (because it is their duty), nor any monetary incentive (because they are publicly funded).

The statutory definition of "person" supports the conclusion that "person" does not include governments. RICO defines "person" to include "any individual or entity capable of holding a legal or beneficial interest in property." 18 U.S.C. § 1961(3). The EC and Departments, of course, are not "individual[s]." In addition, the Second Circuit has concluded that a government is not an "entity" under RICO, explaining that the fact that a government

> is capable of owning property and is, perhaps, an "entity" is no better than ambiguous evidence on this issue since statutory provisions which are written in such general language as to make them reasonably susceptible to being construed as applicable both to the government and to private parties are subject to a rule of construction which exempts the government from their operation in the absence of other particular indicia supporting a contrary result in particular instances.

Bonanno, 879 F.2d at 23 (citations omitted). Other courts have reached similar conclusions. *See Citizens Council of Delaware County v. Brinegar*, 741 F.2d 584, 590-91 (3d Cir. 1984) ("organization" does not include governmental bodies); *In re Davis*, 899 F.2d 1136, 1143-45 (11th Cir. 1990) (same).

2. Rules of Statutory Interpretation Counsel Limiting the Definition of "Person" to Exclude Foreign Governmental Bodies

The context in which "person" is used, together with the statutory "company it keeps," also shows that the term as used in the RICO statute does not include governments. *See, e.g., Jarecki v. G.D. Searle & Co.*, 367 U.S. 303, 307 (1961); *accord Gutierrez v. Ada*, 528 U.S. 250, 255 (2000) (same); *accord Cooper Corp.*, 312 U.S. at 606 ("The connotation of a term in one portion of an Act may often be clarified by reference to its use in others."). Throughout the statute, whenever Congress intended to refer to a governmental actor, it did so by name, not by the term "person." For example, "the subsections immediately preceding and following 1964(c)" expressly identify governmental actors by name. *Bonanno*, 879 F.2d at 22. Subsection 1964(b) provides that "[t]he Attorney General may institute proceedings under this section," and subsection 1964(d) provides that final judgments in criminal proceedings have estoppel effects "in any subsequent civil proceeding brought by the United States." 18 U.S.C. §§ 1964(b), (d). *See also* 18 U.S.C. §§ 1963(c), (d), 1965(c), 1966, 1964 (using term "United States"); § 1961(2) (defining "State"); §§ 1961(6), 1963(a) (using term "State"); § 1961(10) (defining "Attorney General"); § 1963(f), (g) (using term "Attorney General"). Courts will not interpret a statutory term in a way that makes other terms superfluous. *See Ratzlaf v. United States*, 510 U.S. 135, 141 (1994) (rejecting interpretation that would render one part of the statute superfluous). In view of the repeated references to specific governmental actors, it blinks at reality, to say nothing of common sense, to suggest that Congress also intended the term "person" to encompass governmental bodies.

RICO's legislative history leads to the same conclusion. The legislative history offers no indication that RICO's use by or against foreign governments was before Congress, was raised by Congress, or was even debated by Congress. Surely such a significant issue – had it been intended – would have been discussed. Yet it was not. "[I]f Congress had such an intent, Congress would have made it explicit in the statute, or at least some of the Members would have identified or mentioned it at some point in the unusually extensive legislative history . . . ." *Chisom v. Roemer*, 501 U.S. 380, 396 (1991) (declining an expansive interpretation of Voting Rights Act); *see also American Hosp. Ass'n. v. NLRB*, 499 U.S. 606, 613-14 (1991) (declining to interpret NLRB statute as imposing a limitation where no evidence of such intent existed). Congress's conspicuous silence confirms the implausibility of construing "person" to allow treble-damages actions to be brought either by or against governmental bodies.

3. Congress Could Not Have Intended to Give Foreign Governments a Treble-Damage Remedy Unavailable to the United States

There is no basis in logic or common sense to believe that Congress would have intended to make a treble-damage remedy available to foreign governments but not to our own Government. *See Bonanno*, 879 F.2d at 21-26 (holding that United States is not a person entitled to bring treble-damage RICO action). The same reasons for excluding the United States – that it needs no treble-damage incentive to prosecute RICO violations and that it has not consented to be sued for treble damages – applies equally to foreign sovereigns. Furthermore, foreign sovereigns have their own judicial and administrative systems for prosecuting and recovering for RICO-type violations. There is no need to

use the United States courts to do so, except to profit from treble damages – something we do not allow our own government to do.

4. Foreign Sub-Governmental Bodies Have No Standing to Bring Any Action in a United States Court

There is no indication in RICO's statutory language or legislative history that Congress intended the statute to apply to sub-governmental bodies of a foreign government such as the Colombian Departments. Even the few decisions that have held that recognized foreign governments are "persons" under the antitrust laws (*see Pfizer*, 434 U.S. at 320) and RICO (*see Attorney General of Canada*, 103 F. Supp. 2d at 150), have not suggested that political subdivisions of a foreign government, such as the Departments, may be "persons" under RICO. Nor has any court read *Pfizer* to permit non-recognized foreign sub-governmental bodies to bring RICO claims. The reason is simple: foreign sub-governmental bodies do not have standing to bring *any* sovereign claims – RICO or otherwise – in United States courts. Thus, Congress would have had no reason to consider the question, let alone allow such bodies to sue under RICO.

* * *

In short, the United States government could not bring a civil RICO action to collect unpaid taxes on goods entering this country. There is no clear indication that Congress intended foreign governmental bodies to bring such suits. This Court should dismiss plaintiffs' Complaints for failure to state a claim under RICO section 1964(c).

II. RICO DOES NOT APPLY TO THIS PREDOMINANTLY FOREIGN DISPUTE

A. RICO Does Not Apply Extraterritorially

"It is a longstanding principle of American law that legislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States." *EEOC v. Arabian Am. Oil Co.*, 499 U.S. 244, 248 (1991) (citations omitted) (hereinafter "*Aramco*"); *accord Smith v. United States*, 507 U.S. 197, 203-04 (1993). Unless Congress clearly expresses the intent that a statute apply extraterritorially the court must presume it "is primarily concerned with domestic conditions." *Aramco*, 499 U.S. at 248. "Plaintiffs carry the burden of demonstrating a Congressional purpose to overcome the presumption against extraterritorial application." *Labor Union of Pico Korea, Ltd. v. Pico Products, Inc.*, 968 F.2d 191, 194 (2d Cir. 1992) (citing *Aramco*). That is a burden that plaintiffs cannot meet in this case.

"The Supreme Court's recent discussions of the presumption against extraterritoriality seem to require that all statutes, without exception, be construed to apply within the United States only, unless a contrary intent appears." *Kollias v. D & G Marine Maint.*, 29 F.3d 67, 71 (2d Cir. 1994) (citing *Aramco* and *Smith*); *see also Sale v. Haitian Ctrs. Council, Inc.*, 509 U.S. 155, 173-74 (1993) (subjecting Immigration and Nationality Act to presumption and refusing to apply it extraterritorially). The Second Circuit routinely relies upon the presumption against extraterritoriality and holds that the presumption prohibits the extraterritorial application of a statute unless the plaintiff can establish clear Congressional intent to regulate outside U.S. borders. *See, e.g., United States v. Gatlin*, 216 F.3d 207, 212 n.6 (2d Cir. 2000) (taking issue with lower court's refusal to subject 18 U.S.C. §§ 7(3), 2243(a) to the presumption and finding presumption

was not overcome); *Pico Products, Inc.*, 968 F.2d at 195 (subjecting 29 U.S.C. § 185 (Labor Management Relations Act) to the presumption and finding it did not apply extraterritorially); *United States v. Javino*, 960 F.2d 1137, 1142 (2d Cir. 1992) (applying presumption and finding 26 U.S.C. § 5822 (possession of a destructive device) did not apply extraterritorially); *accord Hammell v. Banque Paribas*, 780 F. Supp. 196, 200 (S.D.N.Y. 1991) (applying presumption to state statute).

Applying the presumption here mandates dismissal of the Colombian and EC Actions because nothing in RICO's statutory language or legislative history overcomes the presumption that Congress did not intend the statute to apply extraterritorially.

1. RICO's Statutory Language Contains No Indication That the Statute Was Intended to Apply Extraterritorially

"The RICO statute is silent as to any extraterritorial application." *North South Fin. Corp. v. Al-Turki*, 100 F.3d 1046, 1051 (2d Cir. 1996); *accord Alfadda v. Fenn*, 935 F.2d 475, 479 (2d Cir. 1991). Thus, the presumption against extraterritoriality can be overcome only if some other clear language or indication in the statute reveals that Congress intended to apply the statute extraterritorially. But nothing in RICO's language reflects any intent by Congress to apply the statute extraterritorially. The statute's only reference to "foreign" activities is the statute's requirement that the alleged misconduct affect "interstate or foreign commerce." 18 U.S.C. § 1962(a). The Supreme Court, however, has "repeatedly held that even statutes that contain broad language in their definitions of 'commerce' that expressly refer to 'foreign commerce' do not apply abroad." *Aramco*, 499 U.S. at 251; *Kollias*, 29 F.3d at 73 ("[S]uch broad jurisdictional terms, which form boilerplate language in numerous congressional enactments, are

insufficiently clear expressions of intent to overcome the presumption against extraterritoriality."). Hence, nothing in the RICO statute reveals an intent that it applies abroad.

Indeed, the language of the RICO statute reveals a contrary intent. For example, under RICO, a defendant may be served only in "the United States." 18 U.S.C. § 1965. In contrast, under the antitrust laws, after which RICO was modeled, service can be made wherever a defendant "may be found." 15 U.S.C. § 22. In light of that critical difference, the presumption against extraterritoriality, "far from being overcome here, is doubly fortified by the language of the statute." *Smith*, 507 U.S. at 204 (citations omitted).

2. RICO's Legislative History Contains No Indication that the Statute Was Intended to Apply Extraterritorially

There is nothing in RICO's legislative history to suggest that Congress intended to give RICO extraterritorial effect. In fact, the legislative history suggests just the opposite. RICO's *Statement of Findings and Purpose*, for instance, provides that "(1) organized crime in the United States is a highly sophisticated, diversified, and widespread activity that annually drains billions of dollars from America's economy"; "(4) organized crime activities in the United States weaken the stability of the Nation's economic system . . . seriously burden interstate and foreign commerce, threaten the domestic security, and undermine the general welfare of the Nation and its citizens;" and it is the declared purpose of Congress "to seek the eradication of organized crime in the United States." 1970 U.S.C.C.A.N. at 1073 (emphasis added); *see also United States v. Turkette*, 452 U.S. 576, 589 (1981) (Congress's purpose in enacting RICO was "to seek the

eradication of organized crime in the United States") (quoting same). As a result, in *Jose v. M/V Fir Grove*, 801 F. Supp. 349 (D. Or. 1991) – the only case that has squarely addressed the presumption against extraterritoriality under RICO – the court rejected extraterritorial application of the statute. *Jose*, 801 F. Supp. at 357.[15] The same conclusion should be reached here. And this Court should find that plaintiffs' claims fall outside the statutory scope of RICO and fail to state a claim.

B. Even If RICO Could in Some Conceivable Case Be Applied Extraterritorially, the Allegations of the Complaints Do Not Support Extraterritorial Application

Even if RICO could be applied extraterritorially, the Court would still have to "ascertain whether Congress would have intended that federal courts should be concerned with the specific international controversies" in these particular cases. *North South*, 100 F.3d at 1051 (internal quotations omitted). As Judge Friendly explained:

> When, as here, a court is confronted with transactions that on any view are predominantly foreign, it must seek to determine whether Congress would have wished the precious resources of the United States courts . . . to be devoted to them rather than leave the problem to foreign countries.

[15] The Second Circuit has not yet applied the presumption against extraterritoriality to RICO. Indeed, the only Second Circuit cases to address extraterritorial claims under RICO are *United States v. Parness*, 503 F.2d 430 (2d Cir. 1974), *Alfadda v. Fenn*, 935 F.2d 475 (2d Cir. 1991), and *North South Fin. Corp. v. Al-Turki*, 100 F.3d 1046 (2d Cir. 1996). *Parness* was decided long before *Aramco* and never addressed the presumption against extraterritoriality and appears only to have applied the effects test for subject matter jurisdiction. Relying on *Parness*, the court in *Alfadda* likewise did not apply the *Aramco* decision and was decided before the *Aramco* presumption took hold in other Supreme Court cases, and before *Aramco* began to be applied routinely in the district courts. Finally, in *North South* the Second Circuit did not address the presumption under *Aramco* because the case was dismissed as a threshold matter for lack of subject matter jurisdiction under the conduct and effects tests. Relying on these three decisions, district courts too have failed to apply the *Aramco* analysis to RICO and instead addressed only the subject matter jurisdiction issue under the conduct and effects tests. *See Madanes v. Madanes*, 981 F. Supp. 241, 250 (S.D.N.Y. 1997). In other contexts, however, the Second Circuit has recognized the need to apply the *Aramco* analysis, particularly where prior decisions failed to apply the presumption against extraterritoriality. *See Gatlin*, 216 F.3d at 213-14.

Bersch v. Drexel Firestone, Inc., 519 F.2d 974, 985 (2d Cir. 1975); *see also Butte Mining PLC v. Smith*, 876 F. Supp. 1153, 1161 n.33 (D. Mont. 1995), *aff'd*, 76 F.3d 287 (9th Cir. 1996) ("this court must ascertain whether the international transactions at issue are ones Congress would view as warranting the expenditure of American judicial resources.").

In making that determination, the Second Circuit traditionally relies upon two tests: the "effects" test and the "conduct" test. *See, e.g.*, *North South*, 100 F.3d at 1051-53. However, the Second Circuit has recently indicated that the effects test may be more appropriate in a RICO case. *Id.* at 1052 ("[I]t is not at all clear to us that the conduct test, as it has developed in foreign securities fraud cases, governs in cases involving the extraterritorial application of RICO . . . . It may be that the effects-oriented approach borrowed from antitrust cases is an equally or even more appropriate test, especially since the civil action provision of RICO was patterned after the Clayton Act."). Thus, the effects test is the proper one here. But under either test the result would be the same: subject matter jurisdiction is lacking.[16]

1. The Alleged Foreign Smuggling Had No Substantial Effect in the U.S.

Under the "effects test," a court has no jurisdiction over predominantly foreign transactions unless the alleged transactions have substantial and direct adverse effects within the United States. *North South*, 100 F.3d at 1052. Remote or indirect effects in the United States are insufficient. *See id.* at 1051. Plaintiffs do not allege that the

[16] Because the effects test and the conduct tests are "borrowed" from antitrust and securities fraud cases, respectively, "guidance is furnished by precedents concerning subject matter jurisdiction for international securities transactions and antitrust matters." *North South*, 100 F.3d at 1051.

purported RICO violations had any substantial effect in the United States. Nor could they.

The law is well-settled: where plaintiffs are non-U.S. residents at the time of their injury, effects-based jurisdiction can never exist. Without exception, courts in this Circuit have held that effects-based jurisdiction is lacking where, as here, plaintiffs are non-U.S. residents at the time of their injury. *See, e.g.*, *Europe and Overseas Commodity Traders, S.A. v. Banque Paribas London*, 147 F.3d 118, 128 n.12 (2d Cir. 1998) ("U.S. residence of individual investors . . . must be the focus of the effects test."); *North South*, 100 F.3d at 1052 ("district court was without jurisdiction over a controversy involving foreign victims who sold a foreign entity to foreign defrauders in a foreign transaction lacking significant and material contact with the United States."); *ITT v. Vencap, Ltd.*, 519 F.2d 1001, 1017 (2d Cir. 1975) ("Congress intended the Exchange Act to have extraterritorial application in order to protect domestic investors who have purchased foreign securities . . . .") (citation omitted); *Alfadda v. Fenn*, 966 F. Supp. 1317, 1336 (S.D.N.Y. 1997) (rejecting effects-based jurisdiction where, *inter alia*, the "only allegedly harmed creditors are foreign nationals"); *Koal Indus. Corp. v. Asland, S.A.*, 808 F. Supp. 1143, 1155-56 (S.D.N.Y. 1992) ("Even if the stock of [corporations] had been sold to citizens of the United States, only those citizens, not [a foreign entity who purchased stock], would have standing to seek the extraterritorial protection of the United States securities laws"); *Peters v. Welsh Dev. Agency*, No. 86 C 2646, 1991 WL 172950, *1, *6 (N.D. Ill. Aug. 29, 1991) (dismissing securities fraud and RICO claims where foreign plaintiff "failed to allege any resulting harm to the interests of an American entity or, more generally, to the interest of any foreign entity within the United States.").

Plaintiffs in the present cases are all foreign governmental entities; none was a U.S. resident at the time of its alleged injuries. They complain of injuries (*i.e.*, lost taxes and increased law enforcement costs) that they allegedly sustained outside the U.S. Like every other case involving foreign plaintiffs complaining of a fraud that caused injury abroad, plaintiffs cannot meet their burden of establishing effects-based jurisdiction.

That result is further reinforced by the requirement of the effects test that a defendant have intended its actions to have substantial adverse effects on plaintiffs in the United States. *See, e.g.*, *North South*, 100 F.3d at 1052 ("[L]iability may attach to . . . conduct occurring outside the United States, but having consequences here, if the conduct is intended to and actually does have an effect on [the] United States . . . .") (citing *United States v. Aluminum Co. of Am.*, 148 F.2d 416, 443-44 (2d Cir. 1945) (L. Hand, J.)); *Bersch*, 519 F.2d at 989 (mailing of false prospectus into U.S. "does not support subject matter jurisdiction if there was no intention that the securities be offered to anyone in the United States."). If, as plaintiffs allege, the intent of defendants was to cause harm to foreign entities outside the U.S., there could be no intent to cause a substantial effect on the U.S. Here, plaintiffs allege that defendants operated with the sole purpose of "facilitating" the smuggling of cigarettes into Colombia and Europe. They therefore could not possibly have intended their activity to have a substantial effect on the U.S. The Complaints do not allege any such intent or facts that would support an inference of such intent. Indeed, they allege precisely the opposite – that defendants acted "for the purpose of injuring the economic interest of the Departments of the Republic of Colombia [and the European Community]." (Colom. 2d Am. Compl. ¶ 2; EC Compl. ¶ 2.) Accordingly, plaintiffs cannot satisfy effects-based jurisdiction.

2. The Conduct Material to the Completion of the Alleged Smuggling Schemes Occurred Abroad

In light of the lack of any adverse effect of the alleged smuggling schemes in the United States, the Departments and EC can be expected to urge the Court to apply the "conduct" test to determine whether this Court has subject matter jurisdiction to review their claims. As noted, this Court should find the conduct test inapplicable to RICO cases. *See North South*, 100 F.3d at 1051-53. In any event, even if the conduct test is applied, the Departments and the EC still fail to state a claim.

Under the "conduct" test, a court has subject matter jurisdiction over claims brought by foreign plaintiffs for alleged misconduct occurring principally abroad "only where conduct material to the *completion* of the fraud occurred in the United States." *Id.* at 1051 (quoting *Psimenos v. E.F. Hutton & Co.*, 722 F.2d 1041, 1046 (2d Cir. 1983) (emphasis added)). In applying this standard, courts focus on the final acts necessary to complete the alleged misconduct. Simply engaging in conduct in the United States that facilitates unlawful conduct ultimately completed abroad is insufficient to satisfy the test. *See id*. at 1052-53.

In *Butte Mining PLC v. Smith*, 76 F.3d 287 (9th Cir. 1996), for example, a British corporation allegedly injured by a fraudulent stock swap that occurred in England sued the defendants under RICO in the United States. *Id*. at 288-89. The plaintiffs alleged that the court had subject matter jurisdiction to address the alleged wrongdoing because conduct material to the fraud occurred in the United States. *Id*. at 289-90. The defendants allegedly had purchased land in the United States, formed a United States corporation, and used the United States mails and wires to facilitate the stock trade that occurred overseas. *Id*. at 291.

Although recognizing that the alleged U.S. conduct facilitated the overseas stock trade, the Ninth Circuit stated that the defendants' domestic acts "at most, were steps that the Defendants allegedly took before bringing off the transaction in the United Kingdom." *Id*. As such, these were just acts in aid of misconduct that was completed abroad, and failed to meet the threshold test for subject matter jurisdiction. It is important to note that the court determined that the plaintiffs could not create jurisdiction abroad simply by alleging mail and wire contacts with the United States. *See id*. ("There is no reason to extend the jurisdictional scope of RICO to make criminal the use of the mail and wire in the United States as part of an alleged fraud outside the United States."); *see also North South*, 100 F.3d at 1052 (expressing doubt over application of conduct test where RICO scheme is linked to United States solely by alleged predicate acts of mail and wire fraud). Relying on *Butte Mining*, the Second Circuit in *North South* likewise held that conduct in the United States that at most "facilitated" fraud consummated in France was insufficient to confer jurisdiction on the court. *See North South*, 100 F.3d at 1053.

In the present cases, the alleged fraud was not committed in the United States, but rather was purportedly consummated in Colombia or Europe when unidentified persons and/or entities several times removed from defendants allegedly smuggled cigarettes across the border into foreign territories. While the Complaints allege that defendants engaged in certain conduct in the United States that facilitated the smuggling, such as lawfully selling their products and transmitting sales papers through the mails and wires, defendants here, like the defendants in *Butte Mining* and *North South*, are merely alleged to have engaged in conduct in the United States that was at most preparation of purported

unlawful activities that were completed abroad. So, even accepting plaintiffs' dubious allegations as true for the purpose of these 12(b)(6) proceedings, no alleged unlawful conduct was completed in the United States. Thus, this Court has no subject matter jurisdiction to consider any cause of action based on this alleged misconduct.

III. PLAINTIFFS ALLEGE ONLY DERIVATIVE INJURIES THAT WERE NOT "BY REASON OF" DEFENDANTS' ALLEGED CONDUCT

In order to plead a RICO claim, a plaintiff must allege that its injuries occurred "by reason of" defendants' purported racketeering activity. 18 U.S.C. § 1964(c); *Laborers Local 17 Health and Benefit Fund v. Philip Morris, Inc.*, 191 F.3d 229, 234, 243 (2d Cir. 1999); *Chera v. Chera*, No. 99 Civ. 7101, 2000 WL 1375271, at *4 (E.D.N.Y. Sept. 20, 2000); *Medgar Evers Houses Tenants Ass'n v. Medgar Evers Houses Assocs., L.P.*, 25 F. Supp. 2d 116, 120 (E.D.N.Y. 1998), *aff'd*, 201 F.3d 430 (2d Cir. 1999). A plaintiff's alleged injuries occur "by reason of" a defendant's conduct only if there is a direct link between the injuries and the predicate acts. Here, the claimed injuries, if any, are solely derivative of alleged harm to third parties and therefore could not have occurred "by reason of" defendants' conduct. In addition, the causal link between defendants' sales, the ultimate re-sale, and the alleged smuggling by others into foreign territories is too remote to satisfy the "by reason of" requirement under RICO.

A. Plaintiffs' Alleged Injuries Are Purely Derivative

A plaintiff's alleged injuries are not "by reason of" a defendant's conduct if those injuries are derivative of harm to a third party. *See Laborers Local*, 191 F.3d at 235. As the Second Circuit has explained, "where a plaintiff complains of injuries that are wholly derivative of harm to a third party, plaintiff's injuries are generally deemed indirect and

as a consequence too remote, as a matter of law, to support recovery." *Laborers Local*, 191 F.3d at 236; *accord Chera*, 2000 WL 1375271, at *4. A classic example of a derivative injury is where a shareholder claims that a defendant's RICO violations directed at a corporation caused a diminution in value of the shareholder's stock. "In these cases, the shareholder's injury is only indirect because the decrease in the value of the corporation precipitates the drop in the value of the stock. The corporation, on the other hand, suffers the direct injury in the decreased value of its corporate assets." *Firestone v. Galbreath*, 976 F.2d 279, 285 (6th Cir. 1992); *accord Manson v. Stacescu*, 11 F.3d 1127, 1131 (2d Cir. 1993) ("A shareholder generally does not have standing to bring an individual action under RICO to redress injuries to the corporation in which he owns stock. This is true even when the plaintiff is the sole shareholder of the injured corporation.") (citations omitted); *Jerry Kubecka, Inc. v. Avellino*, 898 F. Supp. 963, 967-68 (E.D.N.Y. 1995) (same).

The shareholder cases are just one example of the derivative injury rule being applied to dismiss RICO claims. *See Laborers Local*, 191 F.3d at 239, 243 (dismissing claims of union trust funds seeking reimbursement for healthcare costs of treating smokers, where losses were contingent upon injuries to individual smokers); *Manson*, 11 F.3d at 1130-32 (dismissing claims of employees and creditors seeking recovery for harm to corporation); *Medgar Evers*, 25 F. Supp. 2d at 123 (dismissing claims of public housing tenants against housing management companies, where target of RICO violations was HUD). Here, any injury to the Departments or EC would be derivative of alleged harm to others – *i.e.*, the Colombian central government and the EC's Member States – which are not parties to these actions.

1. Any Injury to the Departments Is Derivative of Alleged Harms to the Colombian Central Government

The Departments allege that "by reason of" the smuggling of cigarettes into Colombia, they were deprived of taxes that they otherwise would have received. (Colom. 2d Am. Compl. ¶ 45.) But the Departments do not – and cannot – impose their own taxes on imported cigarettes. *See* Colom. Law 223 of 1995, Ch. X, Art. 214.[17] Imposition and collection of cigarette taxes is exclusively the function of the Colombian central government. *See* Colom. Law 223 of 1995, Ch. IX; Colom. Law 30 of 1971. Because any alleged smuggling would have evaded only *national* taxes imposed by the Republic of Colombia, only the Republic, not the Departments, could have suffered direct injury. Consequently, any injury to the Departments would be indirect and – as a matter of law – insufficient to state a claim under RICO section 1964(c).

That the Departments may be the ultimate beneficiaries of some national taxes is of no consequence. Under the Colombian system, national tax revenue on cigarettes is deposited directly into the *Fondo-Cuenta de Impuestos al Consumo de Productos Extranjeros* (the "*Fondo-Cuenta*"), an account under the jurisdiction of the national finance minister. *See* Colom. Law 223 of 1995, Ch. X, Art. 213; Colom. Decree 1640, Art. 10. Pursuant to national law, the revenues deposited in the *Fondo-Cuenta* are later distributed proportionally among the Departments. *See* Colom. Law 223, Ch. X, Art. 217; Colom. Decree 1640, Art. 5. In analogous situations – involving the beneficiaries of other designated funds, like trusts – courts have found RICO standing

[17] *See* Fed. R. Civ. P. 44.1 (permitting Court to consider "any relevant material or source" in determining foreign law).

lacking. In *Firestone v. Galbreath*, for example, beneficiaries of a trust fund claimed that the defendants stole money from the creator of the trust. *See Firestone*, 976 F.2d at 284. This conduct allegedly decreased the value of the trust-creator's net worth, thereby reducing the assets available for deposit into the trust fund from the creator's estate. *See id.* The court first noted that only the trust itself, and not its individual beneficiaries, could sue for losses to the trust corpus. *See id.* The court then held that *even if* the trust itself had sued, its RICO claims would be dismissed for want of standing under the derivative injury rule:

> The relationship between the [plaintiffs'] alleged injury and the injurious conduct here parallels that of the injured stockholders. The [plaintiffs] allege that by stealing from [the trust-creator] during her lifetime, the defendants decreased the size of [her] estate, and consequently the size of their inheritance. This is only an indirect injury because any harm to the [plaintiffs] flows merely from the misfortunes allegedly visited upon [the trust-creator] by the defendants. The estate suffered the direct harm; it, not the Family Trust, lost the property. Consequently, the [Family Trust beneficiaries] lack standing to bring an individual RICO claim, and the district court correctly dismissed it.

Id. (citation omitted).

Just as in *Firestone*, the Departments claim that a fund created for their benefit was deprived of assets because of harm to a third party – the Republic of Colombia – that created the fund. And also as in *Firestone*, any injury to the Departments – indeed, any injury to the *Fondo-Cuenta* itself – is derivative of harm to the Republic of Colombia.

In short, the "hundreds of millions of dollars" in losses supposedly suffered by the Departments are contingent upon – and derivative of – harm to the Republic of Colombia in the first instance and to the *Fondo-Cuenta* in the second instance.

Accordingly, the Departments' claim under RICO section 1964(c) is barred by the derivative injury rule.

2. Any Injury to the EC Is Derivative of Alleged Harm to the Member States

As noted, the EC has suffered no injury at all, let alone a derivative injury. Under the EC tax system, any shortfall to the EC's budget as a result of smuggling or any cause must be paid by the Member States. *See* Council Regulation 1150/2000, of 22 May 2000, Implementing Decision 94/728/EC, Euratom on the System of the European Communities' Own Resources, arts. 5, 17, 2000 O.J. (L 130) 3, 8. The only possible way the EC could claim a loss would be if the Member States violated EC law and failed to cover a budgetary shortfall. *Id.*; *accord* Case 68/88, *Commission v. Hellenic Republic*, 1989 E.C.R. 2945 (1989).[18] The EC has not alleged that the Member States have failed to meet budgetary shortfalls. Moreover, even if a Member State were to do so, then the EC would first have to pursue that loss under EC law. *See Goldfine v. Sichenzia*, 118 F. Supp. 2d 392, 397 (S.D.N.Y. 2000) (plaintiffs failed to show that they were "injured" under RICO as a result of fraudulently induced loans because they had not established that the loans were uncollectable through usual legal means); *accord First Nationwide Bank v. Gelt Funding Corp.*, 27 F.3d 763, 768-69 (2d Cir. 1994) (same). And even if the EC was unable to collect the shortfall pursuant to EC law, its budgetary injuries would still not be cognizable under RICO because such injuries would be contingent upon losses to the Member States, and therefore barred by the derivative injury rule. *See*

[18] Of course, in that event, the suit would have to be filed by the EC in the EC Court of Justice against the offending Member State. EC Treaty art. 226.

Holmes v. Securities Investor Prot. Corp., 503 U.S. 258, 269-70 (1992) (claims that RICO predicate acts caused insolvency of brokerage house thereby preventing payment by brokerage to customers failed to state a claim); *Manson*, 11 F.3d at 1131-32 (claims that RICO predicate acts injured debtor thereby preventing payment to creditors failed to state a claim); *Mid-State Fertilizer Co. v. Exchange Nat'l Bank*, 877 F.2d 1333, 1337-40 (7th Cir. 1989) (same for claims by guarantors).

B. Plaintiffs' Alleged Injuries Are Too Remote

In *Holmes v. Securities Investor Prot. Corp.*, 503 U.S. 258 (1992), the Supreme Court held that civil RICO claims may be barred when, *inter alia*, it is difficult to "ascertain the amount of a plaintiff's damages attributable to the violation, as distinct from other, independent, factors." *Id*. at 269-70; *accord Laborers Local*, 191 F.3d at 236-37; *Medgar Evers*, 25 F. Supp. 2d at 121. In *Holmes*, the plaintiffs, customers of two defunct brokerage houses, alleged that defendants' RICO violations drove the houses into insolvency. The insolvency allegedly prevented the houses from satisfying financial obligations to the plaintiff-customers. The Supreme Court determined that it was impossible to ascertain to what extent the RICO conduct caused the insolvency, "as opposed to, say, the broker-dealers' poor business practices or their failures to anticipate developments in the financial markets." *Holmes*, 503 U.S. at 273; *see also Medgar Evers*, 25 F. Supp. 2d at 121 ("If this RICO claim proceeds, the fact-finder would be required to determine whether the complained of conditions at the Medgar Evers Houses in fact resulted from the false statements to HUD, as opposed to, for example, the defendants' poor management of the housing project.").

As in *Holmes*, it would be impossible to determine whether the Departments' and the EC's alleged injuries were attributable to defendants' purported conduct as opposed to other independent factors, such as plaintiffs' own conduct or the intervening illegal conduct of third parties. In both actions, for example, the Court would have to determine whether the alleged smuggling was caused by defendants' conduct that purportedly made it "more difficult" for authorities to discover smuggling, or whether the smuggling was the result of other factors such as political decisions by the Colombian government or the EC to ineffectively police and enforce smuggling laws, to impose unduly high excise taxes, to proceed with antiquated customs and transit procedures, to engage in government corruption, or to create special customs zones in areas plagued by contraband products. *See Holmes*, 503 U.S. at 273. Moreover, it would be impossible to determine whether defendants' conduct or the intervening criminal acts of third parties caused plaintiffs' alleged losses.

A recent case from the Southern District of New York is instructive on these issues. In *Amsterdam Tobacco, Inc. v. Philip Morris Inc.*, 107 F. Supp. 2d 210 (S.D.N.Y. 2000), the court dismissed a RICO action alleging an *intrastate* smuggling scheme substantially similar to those alleged here. There, the plaintiffs, cigarette wholesalers from New York, claimed that a cigarette manufacturer sold cigarettes to Virginia retailers knowing that these retailers would, in turn, sell the cigarettes to Virginia "middlemen" who were engaged in smuggling. The middlemen allegedly re-sold the cigarettes to "smugglers," who sold them to New York retailers as a means to bypass New York's high cigarette taxes. *See id.* at 212. Like plaintiffs here, the *Amsterdam* plaintiffs alleged

that the defendant-manufacturer should have known that cigarettes that were lawfully sold would be resold to third parties who would seek to avoid taxes. *See id*. at 218.

Although recognizing that the plaintiffs' allegations were "unwarranted," the Southern District held that, even accepting the allegations as true, the alleged smuggling scheme failed to state a claim under RICO. Specifically, the court held that the plaintiffs' losses, if any, were not "by reason of" the alleged knowing sales to smugglers, but by a number of intervening causes, including:

- "the (criminal) smuggling activity by third parties";
- "New York's high rate of taxation relative to that in other states"; and
- "the decision/choice by consumers to purchase cigarettes from retailers other than Plaintiffs."

Id. at 219 n.13. Accordingly, the court concluded that "the (direct) cause of Plaintiffs' lost profits was not any activity of [defendant]. Rather, the 'but for' cause of Plaintiffs' alleged loss was, among other things, the smuggling activity and the decision by New York consumers not to purchase cigarettes from Plaintiffs." *Id.* at 219.

The conspiracies alleged here provide a similarly attenuated chain of causation. As in *Amsterdam*, plaintiffs' alleged tax losses were not "by reason of" defendants' activity, but resulted, if at all, from intervening conduct, including the illegal acts of third party smugglers, ineffective policing by enforcement officials, and the failure of downstream purchasers to pay those taxes.

In sum, there are too many links in the causal chain to support plaintiffs' claims. Under the Departments' and the EC's theory, defendants' lawful sales somehow: (1) caused distributors to sell to smugglers, (2) caused the smugglers to transport the

cigarettes illegally into Colombia or Member States, (3) caused the various customs and policing authorities to fail to detect the smugglers, and (4) caused the cigarette purchasers to break the law and buy contraband cigarettes. *See Laborers Local,* 191 F.3d at 238-40 (illustrating similarly strained chain of causation); *Giro v. Banco Espanol De Credito, S.A.*, No. 99-7883, 2000 WL 287694, at 2-3 (2d Cir. Mar. 17, 2000) (same); *In re Tobacco/Government Health Care Costs Litig.*, 83 F. Supp. 2d 125, 129-31 (D.D.C. 1999) (same); *see also Barr Labs., Inc. v. Quantum Pharmics, Inc.*, 827 F. Supp. 111, 115-16 (E.D.N.Y. 1993) (no RICO standing where harm was dependent upon independent acts of government and customers). Thus, plaintiffs' theory, even if believed, requires the independent criminal acts of unidentified, unnamed, and often unknowable third parties to support their claims, and thus fails to state a claim under RICO.

IV. PLAINTIFFS FAIL TO ALLEGE "A VIOLATION OF SECTION 1962"

The Departments and the EC also fail sufficiently to allege "a violation of section 1962." 18 U.S.C. § 1964(c). Section 1962 has four substantive provisions that generally prohibit defendants from unlawfully investing in, acquiring, establishing, operating or managing an "enterprise" through a pattern of "racketeering activity." *See* 18 U.S.C. § 1962(a)-(d).[19] The Departments and the EC allege violations of all four provisions by

[19] Section 1962(a) makes it unlawful for "any person who has received any income derived . . . from a pattern of racketeering activity . . . to use or invest . . . any part of such income, or the proceeds of such income, in acquisition of any interest in, or the establishment or operation of, any enterprise which is engaged in, or the activities of which affect interstate or foreign commerce." Section 1962(b) makes it unlawful for "any person through a pattern of racketeering activity . . . to acquire or maintain . . . any interest in or control of any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce." Section 1962(c) makes it unlawful for "any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate . . . in the conduct of such enterprise's affairs through a pattern of racketeering activity . . . ." Section 1962(d) prohibits any person from conspiring to violate sections 1962(a), (b), or (c).

each group of defendants, but fail to plead the essential elements necessary to state a claim under any of the provisions.

As a threshold matter, the Departments and EC fail to allege "racketeering activity." RICO expressly defines the offenses that may constitute "racketeering activity" and the Supreme Court recently held that this list is "exhaustive." *Beck v. Prupis*, 529 U.S. 494, 497 (2000). Congress deliberately excluded smuggling and tax offenses from that list. Plaintiffs attempt to overcome that fatal problem by contorting their tax and smuggling claims into claims for mail and wire fraud. However, courts repeatedly have rejected such tactics.

Further, even if smuggling and tax claims could be pleaded as mail and wire fraud offenses, the Colombian and EC Actions fail sufficiently to allege the essential elements of these predicate acts. Recent Supreme Court cases confirm that smuggling does not constitute the type of "scheme or artifice to defraud" covered by the mail and wire fraud statutes and that plaintiffs suffered no deprivation of "property" under those statutes. Plaintiffs also fail to allege the existence of a RICO "enterprise," as defined by the Supreme Court and Second Circuit. Finally, plaintiffs fail to allege other specific requirements of RICO's four substantive provisions under 1962, including the failure to allege the types of injuries necessary to state a claim under sections 1962(a) and (b), the failure to allege any "operation or management" of an enterprise required by section 1962(c), and the failure sufficiently to plead a RICO conspiracy under 1962(d).

A. Smuggling and Tax Evasion Are Not "Racketeering Activity" Under RICO

To state a civil RICO claim under any of RICO's four substantive provisions, a plaintiff must allege that the defendant engaged in a pattern of "racketeering activity." *See* 18 U.S.C. § 1962; *Beck*, 529 U.S. at 497. In RICO section 1961(1), Congress expressly identified over fifty types of predicate criminal acts that may constitute "racketeering activity" under the statute. *See* 18 U.S.C. § 1961(1). The Supreme Court recently confirmed that this list of predicate acts is "exhaustive" and that conduct not on the list is insufficient to support a RICO action. *See Beck*, 529 U.S. at 497 n.2; *accord Red Ball Interior Demolition Corp. v. Palmadessa*, 874 F. Supp. 576, 586 (S.D.N.Y. 1995).

The Departments and the EC allege that defendants engaged in two types of criminal conduct: smuggling and foreign tax evasion. While the United States Code has a number of statutes governing various criminal smuggling and tax offenses,[20] Congress deliberately excluded all smuggling and tax offenses from the list of "racketeering activity" in RICO section 1961(1). *See* 18 U.S.C. § 1961(1). Congress repeatedly has amended section 1961(1) to add or modify listed predicate acts, including adding the crime of *interstate* transportation of contraband cigarettes within the U.S. as a predicate. *See* 18 U.S.C. § 1961(1) (listing 18 U.S.C. §§ 2341-46 as predicates). But Congress has never chosen to make smuggling or tax offenses RICO predicates.

[20] *See, e.g.*, 18 U.S.C. § 545 (inbound smuggling); 18 U.S.C. § 546 (outbound smuggling); 26 U.S.C. §§ 7201 (willful evasion of U.S. tax laws), 7203 (willful failure to file return or to pay tax), 7204 (willfully filing materially false U.S. tax return).

Plaintiffs attempt to avoid that fatal problem by re-packaging their smuggling and tax claims as allegations of mail and wire fraud (18 U.S.C. §§ 1341, 1343), money laundering (18 U.S.C. §§ 1956, 1957), and Travel Act violations (18 U.S.C. § 1952), each of which are predicate acts under section 1961(1). (Colom. 2d Am. Compl. ¶¶ 49(a)-(f), 58, 63, 67 (PM); 126(a)-(f), 135, 138 (BAT Defendants); EC Compl. ¶¶ 43(a)-(f), 52, 56, 61 (PM); 118(a)-(f), 126, 130, 135 (RJR).) However, in recent years,[21] courts repeatedly have rejected similar attempts to "dress up" claims not listed in section 1961(1) as RICO predicates. This court should do the same.

In *Smith v. Jackson*, 84 F.3d 1213 (9th Cir. 1996), for example, the Ninth Circuit affirmed dismissal of a plaintiff's RICO action where the alleged predicate acts were nothing more than non-predicate copyright claims in disguise. *Id*. at 1217 ("Because appellants' RICO counts do no more than allege copyright infringement under the label of mail and wire fraud, and copyright infringement is not a predicate act under RICO, the district court properly concluded that appellants failed to state a claim."); *accord Damiano v. Sony Music Entm't., Inc.*, 975 F. Supp. 623, 632 (D.N.J. 1996) ("Plaintiff's RICO claims must fail because they are actually nothing more than copyright infringement claims presented as mail fraud and copyright infringement is not a predicate act under RICO."); *see also System Mgmt., Inc. v. Loiselle*, 91 F. Supp. 2d 401, 409 (D.

[21] A decade ago, before courts began reeling in the wholesale abuse of the RICO statute, courts tolerated broad interpretation of section 1961(1). *See United States v. Paccione*, 949 F.2d 1183 (2d Cir. 1991). Since then, however, the Supreme Court has reiterated that the list of predicates is "exhaustive" (*Beck*, 529 U.S. at 497 n.2), and courts have rejected plaintiffs' attempts to circumvent the statute by simply disguising non-listed predicates as those included in RICO section 1961(1).

Mass. 2000) (dismissing RICO claim where litigants tried "improperly to fit" unlisted claim under 8 U.S.C. § 1324a into listed claim under 8 U.S.C. § 1324).

Similarly, courts do not allow plaintiffs to transform securities fraud claims into mail and wire fraud in order to circumvent Congress's deliberate removal of securities fraud as a RICO predicate. *See Bald Eagle Area Sch. Dist. v. Keystone Fin., Inc.*, 189 F.3d 321, 330 (3rd Cir. 1999) ("[A] plaintiff cannot avoid the RICO Amendment's bar by pleading mail fraud, wire fraud and bank fraud as predicate offenses in a civil RICO action if the conduct giving rise to those predicate offenses amounts to securities fraud. Allowing such surgical presentation of the cause of action here would undermine the congressional intent behind the RICO Amendment."); *Burton v. Ken-Crest Servs., Inc.*, No. 00CV3205, 2001 WL 21493, at *3-4 (E.D.Pa. Jan. 9, 2001) (same).

Permitting the Departments and the EC to bypass RICO's exclusion of smuggling and tax evasion as predicate acts would likewise undermine the intent of Congress. Confirming the point, the government given the greatest responsibilities for implementing RICO – the United States – has disclaimed any general authority to prosecute RICO claims for tax losses. In the view of the Department of Justice, "[t]ax offenses are not predicates for RICO offenses – a deliberate Congressional decision – and charging a tax offense as a mail fraud charge could be viewed as circumventing Congressional intent unless unique circumstances justifying the use of a mail fraud charge are present . . . . Congress intended that tax crimes be charged as tax crimes . . . when essentially tax law violation motives are involved, even though other crimes may technically have been committed." United States Attorneys' Manual 6-4.211 (Oct. 1997); *accord Fawaz*, 1988 WL 44736, at *2 (a sovereign cannot use RICO to collect

unpaid taxes). What is true for the United States certainly must be true for the Departments and the EC. Surely foreign governmental bodies may not bring a RICO claim that the very government that enacted RICO disclaims any power to bring.

Moreover, allowing smuggling offenses to be contorted into claims for mail and wire fraud would undermine the purpose underlying 18 U.S.C. § 546, the federal outbound smuggling statute. Specifically, section 546, the only provision of the U.S. Code that criminalizes the smuggling of goods *from* the United States *into* another country, expressly provides that such conduct violates U.S. law only if the countries to which the goods are smuggled have reciprocal laws that prohibit outbound smuggling into the United States. *See* 18 U.S.C. § 546. Section 546 was enacted to entice other countries to enact legislation that would prohibit smuggling from other countries into the U.S. *See* H.R. Rep. No. 74-868, at 2-3 (1935); S. Rep. No. 74-1036, at 2-3 (1935). To allow a plaintiff to convert outbound smuggling offenses into claims for mail and wire fraud would not only circumvent RICO, it would undermine the primary purpose of section 546. *See United States v. Boots*, 80 F.3d 580, 588 (1st Cir. 1996) (finding that section 546 cannot be pleaded as mail fraud).

In sum, "Congress painstakingly enumerated a complete list of predicate acts in 18 U.S.C. § 1961(1)." *Miranda v. Ponce Fed. Bank*, 948 F.2d 41, 48 (1st Cir. 1991). Plaintiffs cannot circumvent the requirements of RICO simply by disguising their tax and smuggling claims as qualifying predicate acts.

B. The Alleged Predicate Acts Fail to State a Claim and Are Therefore Insufficient to Constitute "Racketeering Activity"

1. Plaintiffs Fail to Plead the Essential Elements of Mail and Wire Fraud

The mail and wire fraud statutes relied upon by plaintiffs to plead "racketeering activity," prohibit the use of the mail or wires in furtherance of (1) "any scheme or artifice to defraud" that (2) causes the victim to relinquish "money or property." *See* 18 U.S.C. §§ 1341, 1343. The alleged "scheme or artifice to defraud" here is "smuggling" and the alleged "property" interests are unpaid taxes and duties. Two recent Supreme Court cases establish that these allegations are insufficient as a matter of law.

a. Smuggling Is Not A "Scheme or Artifice to Defraud" Covered by the Mail and Wire Fraud Statutes

In *Neder v. United States*, 527 U.S. 1, 21-22 (1999), the Supreme Court unanimously held that the mail and wire fraud statutes are not, as some Circuits had previously held, amorphous general fraud statutes encompassing any and all *conduct* that deprives another of property. *See id* at 24.[22] Rather, the statutes must be more narrowly construed so as to prohibit only that conduct that amounts to "actionable fraud" at common law. *Id.* Thus, the Court held a "scheme or artifice to defraud" under the mail and wire fraud statutes must involve (1) a misrepresentation of fact that is (2) material to the alleged fraud (*i.e.*, capable of influencing the intended victim). *See id.* at 23-24; *see*

[22] Before *Neder*, a few courts had ruled that mail or wire fraud included activity that violates "fundamental notions of honesty, fair play and right dealing," even in the absence of specific misrepresentations or where the misrepresentations were immaterial in influencing the victim's injury. For example, a footnote in *United States v. Trapilo*, 130 F.3d 547, 550 n.3 (2d Cir. 1997), held that smuggling, without an allegation of any misrepresentation, may qualify as a scheme to defraud under the wire fraud statute. *Neder* rejected such an over-broad interpretation of the mail and wire fraud statutes, requiring instead that plaintiffs allege conduct that constituted fraud at common law. *See Neder*, 527 U.S. at 21-24.

also Chanayil v. Gulati, 169 F.3d 168, 171 (2d Cir. 1999) (common law fraud requires misrepresentation and materiality).

Under *Neder*, a scheme to commit a robbery or to steal a car, for example, would not support a mail or wire fraud claim because those offenses are grounded not in misrepresentations of material fact, but in unlawful *conduct*. Similarly, in the present action, smuggling is an offense driven by conduct, not by misrepresentations. *See Gust v. Jones*, 162 F.3d 587, 595 (10th Cir. 1998) (prior smuggling convictions inadmissible for impeachment purposes under Federal Rule of Evidence 609 because smuggling is not a crime involving dishonesty or false statements). The very nature of smuggling is surreptitiously to transport goods across the border so as to avoid making any representations at all. Thus, smuggling is "an act unlikely to constitute an act of common law fraud . . . ." *In re Sumitomo Copper Litig.*, 995 F. Supp. 451, 455 (S.D.N.Y. 1998). As a result, it cannot constitute an "scheme or artifice to defraud" under the federal mail and wire fraud statutes.

b. Plaintiffs Were Not Deprived of Any "Money or Property"

The Supreme Court repeatedly has recognized that the mail and wire fraud statutes are "limited in scope to the protection of property rights." *McNally v. United States*, 483 U.S. 350, 360 (1987); *accord Cleveland v. United States*, 121 S. Ct. 365, 371 (2000). In *Cleveland*, the Supreme Court recently adhered to its strict interpretation of the term "property" under those statutes where the victim of the alleged fraud is a sovereign. The Supreme Court unanimously held that a state does not have a "property" interest in state licenses – even though the licenses generate substantial revenue to the

state – and that false statements made to acquire such licenses were therefore not actionable under the mail and wire fraud statutes. *See id.* at 366-67. The Court emphasized that the mail fraud statute "requires the object of the fraud to be 'property' in the victim's hands . . . ," *id*. at 374, and that an unissued license is not "property" in the hands of the state; it simply "implicates the Government's role as sovereign, not as property holder." *Id.* at 373.

The Court was unmoved by the government's argument that the license constituted "property" because the state "receives a substantial sum of money in exchange for each license and continues to receive payments from the licensee as long as the license remains in effect." *Id*. at 372. Rejecting this argument, the Court declared that the right to collect this revenue does not create a property interest in the hands of the state. *See id*. at 372-73. [23] Rather, the right to collect such revenue, along with the right to control issuance, renewal, and revocation of the license were not property interests, but sovereign interests. Thus, "[e]ven when tied to an expected stream of revenue, the State's right of control [over the issuance of licenses] does not create a property interest any more than a law licensing liquor sales in a State that levies a sales tax on liquor. Such regulations are paradigmatic exercises of the States' traditional police powers." *Id*. at 372-73. The *Cleveland* Court concluded by noting that it is not always clear whether certain interests constitute "property" interests. In those instances, the Court held that when used as RICO predicates the mail and wire fraud statutes should be construed narrowly and all doubts resolved in favor of finding no property interests. *See id.*

[23] Before *Cleveland* was decided, the Second Circuit appeared to hold (2-1) that the right to collect state taxes was a property interest under the mail and wire fraud statutes. *See United States v. Porcelli*, 865 F.2d 1352, 1361 n.2 (2d Cir. 1989).

In the present case, plaintiffs do not claim that any defendant failed to declare or pay taxes due, or that the corporations themselves imported the goods and evaded the taxing authorities. Rather, the Colombian and EC Complaints allege that unnamed third parties – who allegedly smuggled the goods into Colombia or Member States – failed to declare and pay the taxes due at the time of entry. The only "property" interests defendants are alleged to have caused the non-party Republic of Colombia and EC Member States to relinquish are their ability to collect these taxes from the third parties. The Complaints allege that defendants interfered with these collection interests by engaging in conduct that made it "more difficult" for the Colombian and Member State tax officials to collect the taxes due from the third parties who owe them. (Colom. 2d Am. Compl. ¶¶ 32(f)-(h); 37(a), (b), (j), (l), (n), (t), (v) (PM); 38(qq) (BAT Defendants); EC Compl. 27(f)-(h); 32(j), (r) (RJR); 33(b), (i), (j), (l), (n), (o) (PM).)

As recognized by the Supreme Court in *Cleveland*, however, depriving governmental entities of the ability to collect revenues derived from sovereign claims are not "property" interests; they are sovereign interests. Any doubt on this score must be resolved in favor of defendants. *See Cleveland*, 121 S. Ct. at 373. In any event, as noted above, the Departments suffer no direct losses from taxes not paid to the Republic of Colombia and the *Fondo-Cuenta*; and the EC can never suffer any losses from smuggling because all budgetary shortfalls are paid by the Member States. As such, plaintiffs have not relinquished any property, sovereign or otherwise.

2. Plaintiffs' Remaining RICO Predicate Acts Are Legally Insufficient

a. Plaintiffs Fail to Allege Violations of the Money Laundering Statutes

Plaintiffs' money laundering counts are legally deficient. In order to establish money laundering as a RICO predicate act, a plaintiff must plead all essential elements of the offense. *See Ray v. General Motors Acceptance Corp.*, No. 92 Civ. 5043, 1995 WL 151852, at *6 (E.D.N.Y. Mar. 28, 1995). Like RICO, the money laundering statute requires allegations of predicate acts. The money laundering statute expressly incorporates RICO's definition of "racketeering activity" under section 1961(1), and then expands on that list. *See* 18 U.S.C. § 1956(c)(7). The additions, however, do not include any foreign tax or outbound smuggling offenses. *See id.*; *accord* 18 U.S.C. § 1957(f)(3) (incorporating section 1956's list of predicates). Accordingly, for the same reason that plaintiffs fail to allege predicate "racketeering activity" under RICO they fail to allege the necessary predicates for money laundering.

Plaintiffs' money laundering allegations also fail to connect any defendant to the supposed money laundering activities. A claim of money laundering must identify the defendants and the transactions that violated the statutes. The allegations cannot be so "vague [that] it is difficult to find factual support for them in the complaint or attribute them to the defendants." *Bernstein v. Misk*, 948 F. Supp. 228, 236 n.2 (E.D.N.Y. 1997); *accord Zigman v. Giacobbe*, 944 F. Supp. 147, 156 (E.D.N.Y. 1996). That is precisely the problem here.

Plaintiffs make nothing but vague and conclusory assertions, involving unidentified transactions at undisclosed banks by unidentified individuals. (*See* Colom.

2d Am. Compl. ¶ 32(h); EC Compl. ¶ 27(h) (defendants "ma[d]e arrangements for the smuggled cigarettes to be paid for into foreign accounts including Swiss corporations and/or Swiss bank accounts in an attempt to improperly utilize Swiss banking and privacy laws as a shield to protect the smugglers from government investigations concerning their activities.").) Such allegations are too vague to support a RICO claim.

b. Plaintiffs Fail to Allege Violations of the Travel Act

The Travel Act criminalizes travel in or the use of facilities of interstate or foreign commerce with the intent to "distribute the proceeds of any unlawful activity" or to "otherwise promote, manage, establish, carry on, or facilitate . . . any unlawful activity." 18 U.S.C. § 1952 (a)(1) & (3). "Facility of interstate commerce" includes any "means of transportation and communication." 18 U.S.C. §1958(b)(2). "Unlawful activity" for purposes of the Travel Act includes any business enterprise involving narcotics, as well as "any act which is indictable under [the federal money laundering statutes]." 18 U.S.C. § 1952(b)(3). It does not, however, include tax or smuggling offenses.

To plead a Travel Act violation as a RICO predicate act, a plaintiff must allege three essential elements: (1) that the defendant traveled in or used a facility of interstate or foreign commerce; (2) with the intent to distribute the proceeds of unlawful activity, or to facilitate unlawful activity; and (3) thereafter performed an additional act in furtherance of the unlawful activity. *United States v. Salameh,* 152 F.3d 88, 152 (2d Cir. 1998).

The first element – use of an interstate foreign facility –requires that the facility be significantly related to the unlawful activity. *United States v. Muskovsky,* 863 F.2d 1319, 1327 (7th Cir. 1988) (interstate travel or use must relate significantly to the illegal

activity). Incidental, minimal, or fortuitous interstate travel or use of a facility does not violate the Act. *See United States v. Raineri*, 670 F.2d 702, 717 (7th Cir. 1982).

Plaintiffs here fail to plead facts establishing a significant relationship between defendants' alleged use of a facility and the distribution by others of drug proceeds or drug trafficking. Plaintiffs claim that on unspecified occasions, unnamed individuals "solicited contacts with [unidentified] companies and individuals in Central America and the Caribbean that the Defendants knew, or had reason to know, were money launderers" and that "[e]xecutives and employees of [defendants] traveled to the Caribbean and to Central America on multiple occasions for the purpose of meeting and negotiating business agreements with individuals who the . . . defendants knew, or should have known, were involved in the laundering of narcotics proceeds." (EC Compl. ¶ 32(f); *accord* Colom. 2d Am. Compl. ¶ 37(o).) Plaintiffs' allegations merely describe a fortuitous relationship between the alleged interstate travel or use of interstate facilities and money laundering or narcotics trafficking that do not constitute the significant relationship required to state a claim under the Travel Act.

The second element requires that the defendant used facilities of interstate commerce with the specific intent to distribute the proceeds of, or otherwise promote, one of the Act's enumerated "unlawful activit[ies.]" *United States v. Walsh*, 700 F.2d 846, 852-53 (2d Cir. 1983); *United States v. Markowski*, 772 F.2d 358, 364 (7th Cir. 1985). As noted, smuggling and tax offenses are not among those "unlawful activities." This alone mandates dismissal. Moreover, plaintiffs fail to allege the requisite intent under the Act. Intent to promote the alleged unlawful activity exists only if the defendant "in some significant manner associated himself with the [ ] criminal venture for the purpose of its

advancement." *United States v. Gibson Specialty Co.*, 507 F.2d 446, 449 (9th Cir. 1974) (noting that intent under Travel Act was "specific intent to promote, manage, establish, carry on or facilitate one of the prohibited activities."). And where the alleged predicate "unlawful activity" is narcotics activity, a plaintiff must adequately describe a narcotics "business enterprise," which requires allegations describing a "continuous course of conduct, rather than sporadic casual involvement in proscribed activity." *United States v. Davis*, 666 F.2d 195, 201 n.10 (5th Cir. 1982) (citations omitted). Plaintiffs fail to allege specific facts demonstrating that defendants intended to support narcotics activities presumably because they know it is not so. Plaintiffs also fail to plead any fact that would establish a "continuous course of conduct" constituting a narcotics "business enterprise." Rather, the gravamen of the suits is that defendants "facilitated" smuggling by selling their products to customers who may have sold them to others who were involved in smuggling and, incidentally, narcotics activities as well. (Colom. 2d Am. Compl. ¶ 37(i); EC Compl. ¶ 33(g).)

The third element requires that after the defendant traveled in or used interstate facilities, defendant performed or attempted to perform an additional act that furthered the alleged unlawful activity. *United States v. Falcon*, 766 F.2d 1469, 1478 (10th Cir. 1985). Plaintiffs fail to identify a single specific drug transaction or a single individual involved in drug trafficking, much less one which any defendant was aware. Instead, they make general averments about facilitating "drug lords" and that smuggling is linked to the "Black Market Peso Exchange" and "Colombian cocaine smugglers" (Colom. 2d Am. Compl. ¶ 37(o); EC Compl. ¶ 36) that are insufficient under the Travel Act.

3. Plaintiffs' Alleged Injuries Were Not Caused by the RICO Predicate Acts

A RICO plaintiff must allege that its injuries "flow from the commission of the predicate acts." *Sedima S.P.R.L. v. Imrex Co.,* 473 U.S. 479, 497 (1985). The alleged injury must be proximately caused by the predicate acts, not by other conduct of the defendant or the enterprise. *See Hecht v. Commerce Clearing House, Inc.*, 897 F.2d 21, 23-24 (2d Cir. 1990). Moreover, where the predicate acts are mail and wire fraud, a plaintiff's injuries must have resulted from its *reasonable reliance* on the fraudulent communications. *See Piccone v. Board of Directors of Doctors Hosp*., No. 97 Civ. 8182, 2000 WL 1219391, at *5 (S.D.N.Y. Aug. 28, 2000) ("If one alleges predicate acts of mail fraud, as [plaintiff] does, 'it is necessary to allege that the injured party relied on the fraudulent misrepresentations of the defendant, and that the reliance was the cause of the injury.'"); *accord Metromedia Co. v. Fugazy,* 983 F.2d 350, 368-69 (2d Cir. 1992); *Summit Properties, Inc. v. Hoechst Celanese Corp.*, 214 F.3d 556, 559 (5th Cir. 2000); *Red Ball*, 874 F. Supp. at 586-87. As discussed below, plaintiffs fail sufficiently to allege any reasonable reliance on the alleged mail and wire communications. They also fail to allege any other injuries flowing from the other predicate acts.

a. Plaintiffs Did Not Rely on Defendants' Alleged Mail and Wire Communications

The Departments and the EC strain to bring defendants' alleged conduct within the scope of the federal mail and wire fraud statutes. Recognizing that they must establish that they were injured by their reliance on alleged misrepresentations made by

defendants, the Departments and the EC generate several tenuous alleged misrepresentations upon which they purportedly relied:

- **"False" Shipping Papers and Packaging –** Defendants allegedly made misrepresentations or omissions in sales and transit papers and cigarette packaging, which supposedly hindered the ability of customs officials to track the purported "ultimate destination" for such sales, making it more difficult for policing authorities to detect smuggling. (Colom. 2d Am. Compl. ¶ 37(nn); EC Compl. ¶ 34(e) (PM); Colom. 2d Am. Compl. ¶ 38(qq) (BAT Defendants); EC Compl. ¶ 32 (aa) (RJR).)

- **"False" Denials Made in Public Statements –** Defendants allegedly used the mails and wires in communications with various third parties, like the Center for Public Integrity and several newspapers, in which they "falsely denied" that they were involved in smuggling. (Colom. 2d Am. Compl. ¶ 37(w), (tt), (uu); EC Compl. ¶ 34(j)-(k) (PM); Colom. 2d Compl. ¶ 38(xx)-(yy) (BAT Defendants); EC Compl. ¶ 32(p) (RJR).)

- **"False" Challenges to Plaintiffs' Legal Theories –** Defendants somehow caused plaintiffs' alleged tax losses by making "false statements" that plaintiffs' legal claims lack merit. (Colom. 2d Am. Compl. ¶ 37(vv).)

- **Undervaluation –** The Departments also claim that they were injured by Philip Morris' and the BAT Defendants' alleged under-valuation of lawfully imported cigarettes. (Colom. 2d Am. Compl. ¶¶ 37(e) (PM); 38(c) (BAT Defendants).)

Those allegations are legally insufficient. As an initial matter, given the variables at play in government decision making, statements to government authorities cannot – as a matter of law – be the proximate cause of alleged injuries caused by government inaction. *See In re Tobacco/Governmental Health Care Costs Litig.*, 83 F. Supp. 2d at 130 (misrepresentations to government entities are legally insufficient to have caused government inaction because of the "great number of subjective influences at play" in government decision-making); *Barr Labs.*, 827 F. Supp. at 116 (false statements to FDA not cause of harm dependent on FDA's response to predicate acts).

Further, plaintiffs fail to plead reliance because they claim only that the alleged statements made it "more difficult" to prevent or discover the alleged smuggling schemes. As a matter of law, these allegations are insufficient. *See Red Ball*, 874 F. Supp. at 586-87; *Miller v. Mitnik*, No. 94 Civ. 757, 1997 WL 1048902, at *6 (E.D.N.Y. Mar. 31, 1997). In *Red Ball*, for example, the plaintiff asserted that the defendants' fraudulent mail and wire communications kept the plaintiff from "more effectively" preventing further unlawful conduct by the defendants. *See Red Ball*, 874 F. Supp. at 587. The court held that this left open the possibility that plaintiff's injuries could have occurred regardless of the communications, rendering it impossible for the plaintiff to establish that the predicate acts were a substantial factor causing the alleged harm. *See id.*; *accord Miller*, 1997 WL 1048902, at *6. As in *Red Ball*, the communications here are alleged to have done nothing more than make it "more difficult" to discover wrongdoing. (Colom. 2d Am. Compl. ¶ 37(m); EC Compl. ¶ 32(r), 33(l).) That leaves open the possibility – indeed it strongly suggests – that the alleged wrongdoing would have occurred regardless of the alleged communications rendering any claim of reliance on such alleged misrepresentations deficient as a matter of law.

Moreover, plaintiffs as a matter of law cannot have reasonably relied on defendants' alleged public statements and denials and the challenges to plaintiffs' legal theories. A plaintiff's reliance must be *reasonable*. *See Metromedia*, 983 F.2d at 368. It would not have been reasonable for plaintiffs to have suspended efforts to detect smuggling simply because the parties allegedly involved in the claimed misconduct denied involvement in that conduct or criticized the legal theories underlying threatened litigation against them.

Finally, with regard to the alleged "underinvoicing" communications, those alleged misrepresentations were purportedly made only to the Republic's customs officials, not the Departments. In any event, there is litigation currently pending in Colombia involving the appropriate valuation standard for imported products. A central issue in those cases is whether valuation should accord with the World Trade Organization ("WTO") valuation agreement that has been incorporated into Colombian law, or whether valuation must be done pursuant to a contradictory method used by the Republic of Colombia's Customs and Tax Authority. The Colombian courts have yet to rule on these issues. As a matter of law, plaintiffs cannot sufficiently plead intent to defraud, where, as here, a defendant is alleged to have relied on a reasonable interpretation of a disputed law. *Cf. Hagood v. Sonoma County Water Agency*, 81 F.3d 1465, 1478-79 (9th Cir. 1996) (defendant could not have made "false" cost allocations under the False Claims Act where the method for calculating allocations was unclear; "[a]t most, [plaintiff] has shown that the Water Agency took advantage of a disputed legal issue. This, as we have previously held, is not enough" to establish fraud.).

b. The Alleged Travel Act and Money Laundering Predicates Could Not Have Caused Injury to Plaintiffs

"An act which proximately caused an injury is analytically distinct from one which furthered, facilitated, permitted or concealed an injury which happened or could have happened independently of the act." *Red Ball*, 874 F. Supp. at 587; *see also Moeller v. Zaccaria*, 831 F. Supp. 1046, 1054 (S.D.N.Y. 1993). Plaintiffs' Travel Act and money laundering predicates ignore that distinction. The Travel Act and money laundering counts allege only that defendants accepted, transported, and concealed funds

derived from the illegal acts of third party smugglers. (Colom. 2d Am. Compl. ¶¶ 49, 53, 62 (PM); 126, 135, 139 (BAT Defendants); EC Compl. ¶¶ 43, 52, 56 (PM); 118, 126, 130 (RJR).) Plaintiffs fail to allege how receiving and concealing any such funds caused (1) the smugglers illegally to transport cigarettes into Colombia or fail to pay taxes due on those products; (2) the policing authorities to fail to detect the smugglers; or (3) the cigarette purchasers to break the law and buy contraband cigarettes. At best, these alleged predicate acts "facilitated" or "concealed" an injury that could or would have happened independently of the alleged predicate acts. *See Red Ball*, 874 F. Supp. at 587.

C. Plaintiffs Fail to Allege the Existence of a RICO "Enterprise"

To state a claim under RICO section 1962, a plaintiff must allege that the defendants unlawfully invested in, acquired, established, operated or managed an "enterprise" through a pattern of racketeering. *See* 18 U.S.C. § 1962(a)-(d). RICO section 1961(4) defines an "enterprise" as including "any individual, partnership, corporation, association, or other legal entity, and any union or group of individuals associated in fact although not a legal entity." 18 U.S.C. § 1961(4). The Supreme Court has held that an "enterprise" must be an "ongoing organization" functioning as a "continuing unit." *United States v. Turkette*, 452 U.S. 576, 583 (1981).

Plaintiffs allege a separate "association-in-fact" enterprise by each of the three groups of defendants. The Colombian Action includes the "PM Smuggling Enterprise" and the "BAT Smuggling Enterprise." (Colom. 2d Am. Compl. ¶¶ 48, 125.) The EC Action includes the "PM Smuggling Enterprise" and the "RJR Smuggling Enterprise." (EC Compl. ¶¶ 42, 117.) Each of these alleged enterprises is defined identically in the Colombian and EC Complaints as a "vertical group" which consists of defendants,

unnamed distributors, shippers, smugglers, and currency brokers "who received payment for the cigarettes, . . . engag[ed] in a course of conduct to gain massive profits from the sale of cigarettes that were illegally sold in the Departments [and EC]." (Colom. 2d Am. Compl. ¶ 36; EC Compl. ¶ 31.)

These "enterprise" allegations are insufficient as a matter of law. As a threshold matter, nothing in the Colombian or EC Complaints differentiates the alleged "vertical group" from the alleged "pattern of racketeering." *Turkette*, 452 U.S. at 583. The Supreme Court has made clear that "the 'enterprise' is not the 'pattern of racketeering activity;' it is an entity separate and apart from the pattern of activity in which it engages." *Id.* The problem in the present cases is that each enterprise allegedly had a single purpose – smuggling. If the predicate acts in furtherance of that alleged purpose are taken away, no association, in law or fact, remains. *See Schmidt v. Fleet Bank*, 16 F. Supp. 2d 340, 350 (S.D.N.Y. 1998) (single purpose enterprises have no continuity or structure beyond the alleged conspiracy); *accord Bank v. Brooklyn Law Sch.*, No. 97 Civ. 7470, 2000 WL 1692844, at *4-6 (E.D.N.Y. Oct. 6, 2000). Indeed, in the recent *Amsterdam* case, the court rejected allegations of a "vertical" smuggling enterprise nearly identical to those in these actions. *See Amsterdam*, 107 F. Supp. 2d at 215. The court concluded that "[t]he vertical group described by Plaintiff here is merely a reiteration of the (alleged) racketeering activity. Even allowing for the notion that 'enterprise' should be defined 'broadly,' Plaintiff here has failed to allege a RICO enterprise." *Id.* (citations omitted). Likewise, the enterprises and racketeering activities alleged by plaintiffs here are one-and-the-same. For that reason, the Complaints fail to state a claim.

Furthermore, the Complaints fail to identify any ongoing organization that functions as a continuing unit. The Complaints contain no description connecting the alleged smugglers to one another or identifying any chain-of-command or structure of the enterprises. Mere allegations of wrongdoing by an uncoordinated group of individuals who purchased cigarettes from defendants are insufficient to establish an enterprise. *See Cullen v. Paine Webber Group, Inc*., 689 F. Supp. 269, 273 (S.D.N.Y. 1988) (holding no enterprise exists where investment clients "did not share a common purpose or associate together; their only link was their broker."); *First Nationwide Bank v. Gelt Funding Corp.*, 820 F. Supp. 89, 98 (S.D.N.Y. 1993) ("[I]t appears at worst that several borrowers each committed a similar but independent fraud with the aid of a particular lender, and that each such borrower acted on a particular occasion to benefit himself or herself and not to assist any other borrower."), *aff'd*, 27 F.3d 763 (2d Cir. 1994).

In *Stachon v. United Consumers Club, Inc.*, 229 F.3d 673 (7th Cir. 2000), for example, the Seventh Circuit recently dismissed a RICO action that alleged that the "enterprise" was simply a list of participants in the conspiracy without identifying the duration or scope of the enterprise or how the participants operated as an on-going organization other than that they maintained a supplier-distributor relationship. *See id*. at 676 ("[T]he mere fact that [defendant] had business dealings with a wide assortment of unnamed manufacturers, wholesalers, and members in no way establishes that they function with [defendant] as a continuing unit or as an ongoing structured organization.").

The Departments and the EC attempt to salvage their deficient enterprise allegations by restating the legal definition of an "enterprise." (Colom. 2d Am. Compl.

¶¶ 48 (PM); 125 (BAT Defendants); EC Compl. ¶¶ 42 (PM); 117 (RJR).)[24] But as this Court has previously recognized, "bald legal conclusions" cannot resuscitate insufficient enterprise allegations. *See Ray v. General Motors Acceptance Corp.*, No. 92 Civ. 5043, 1995 WL 151852, at *3 (E.D.N.Y. Mar. 28, 1995); *accord Amsterdam*, 107 F. Supp. 2d at 212.

D. Plaintiffs Fail to Plead the Remaining Elements Necessary to State a Claim Under RICO Sections 1962(a) Through (d)

1. Plaintiffs Fail to Plead "Investment Injury" or "Acquisition or Maintenance Injury" Under RICO Sections 1962(a) and (b)

RICO sections 1962(a) and (b) make it unlawful for a party to "invest" the proceeds of racketeering activity in any enterprise or "acquire or maintain" an enterprise through a pattern of racketeering. *See* 18 U.S.C. §§ 1962(a)-(b). These provisions were designed to prevent the infiltration of legitimate businesses through illegal conduct. Accordingly, to state a claim under 1962(a), "it is insufficient merely to allege injuries from the predicate acts. Instead, plaintiff is required to plead a distinct injury from the defendant's investment of the racketeering income in an enterprise." *Soberman v. Groff Studios Corp.*, No. 99 Civ. 1005, 1999 WL 349989, at *5 (S.D.N.Y. June 1, 1999); *accord Ouaknine v. MacFarlane*, 897 F.2d 75, 83 (2d Cir. 1990); *Protter v. Nathan's Famous Sys., Inc.*, 925 F. Supp. 947, 954 (E.D.N.Y. 1996). If a complaint fails to allege

[24] Each enterprise is described as follows:

> The PM [BAT or RJR] Smuggling Enterprise has an ascertainable structure and purpose beyond the scope of the Defendants' predicate acts and the conspiracy to commit such acts, and it possesses an infrastructure and chain of command that is distinct and separate from the corporate structure of the Philip Morris [BAT or RJR] Defendants.

(Colom. 2d Am. Compl. ¶¶ 48 (PM), 125 (BAT Defendants); EC Compl. ¶¶ 42 (PM), 117 (RJR).)

a separate and distinct "investment injury" – an injury flowing from the alleged investment itself and not from the predicate acts – the RICO action must be dismissed for failure to state a claim.

Similarly, a necessary element of RICO section 1962(b) is that a defendant be found to "acquire or maintain" an interest in an enterprise through a pattern of racketeering. *See* 18 U.S.C. § 1962(b). As with section 1962(a), courts require a showing of "acquisition or maintenance injury," and will dismiss a case for failure to state a claim if the complaint does not allege a separate injury directly flowing from the alleged acquisition of the enterprise, as opposed to just from the predicate acts. *See Discon, Inc. v. Nynex Corp.*, 93 F.3d 1055, 1062-63 (2d Cir. 1996), *vacated on other grounds*, 525 U.S. 128 (1998); *Protter*, 925 F. Supp. at 954-55.

Mere allegations of "reinvestment injury," that is, "allegations that investment of the income derived from the pattern of racketeering enabled the defendants to continue their fraudulent behavior will not pass 12(b)(6) muster." *Protter*, 925 F. Supp. at 954; *see also Soberman*, 1999 WL 349989, at *5 ("[T]he mere allegation that the proceeds from the scheme were used to perpetuate the enterprise is insufficient" to state a claim under section 1962(a) or (b)); *Kaczmarek v. IBM*, 30 F. Supp. 2d 626, 628-29 (S.D.N.Y. 1998) ("Mere reinvestment of racketeering income into the same racketeering enterprise that generated the income does not satisfy the Second Circuit's holding in *Ouaknine* because investment of the proceeds from the pattern of racketeering for general operations is too attenuated a causal connection to satisfy sections 1962(a) and 1964(c).").

a. Plaintiffs Allege No Investment Injury And Fail to State A Claim Under Section 1962(a)

Plaintiffs' claims under RICO section 1962(a) fail to allege any distinct investment injury. At best they allege mere "reinvestment" injuries that fail to state a claim. The Colombian Complaint, for example, alleges that Philip Morris and the BAT Defendants violated section 1962(a) because proceeds derived from illegal smuggling were allegedly invested in the "PM Smuggling Enterprise" (Colom. 2d Am. Compl. ¶ 48) and the "BAT Smuggling Enterprise." (Colom. 2d Am. Compl. ¶ 123.) The funds supposedly supported and created "the infrastructure" of the smuggling operations that made possible the continued operation of these separate smuggling enterprises. (Colom. 2d Am. Compl. ¶¶ 54(PM); 131(BAT Defendants).) The EC Complaint makes identical 1962(a) assertions against Philip Morris and RJR. (EC Compl. ¶¶ 48, 123.) The Colombian and EC Complaints do not show any separate or distinct injury deriving from the alleged investments or acquisitions. Instead, the Departments and EC simply (and identically) allege that defendants' conduct facilitated the continuation of the purported misconduct. This merely alleges "re-investment" injury, insufficient to state a claim under section 1962(a). *See Protter*, 925 F. Supp. at 954; *Soberman*, 1999 WL 349989, at *5.

b. Plaintiffs Allege No Acquisition Injury And Fail to State A Claim Under Section 1962(b)

Similarly, plaintiffs allege that defendants violated section 1962(b) because their acquisition of the "PM Smuggling Enterprise," the "BAT Smuggling Enterprise," and the "RJR Smuggling Enterprise" allegedly "furthered, concealed, and protected the operations of the smuggling enterprise, and thereby permitted the [PM, BAT Defendants,

and RJR] Smuggling Enterprise[s] to flourish without detection." (Colom. 2d Am. Compl. ¶¶ 58 (PM); 135 (BAT Defendants); EC Compl. ¶¶ 52 (PM); 127 (RJR).) Again, these claims are for reinvestment injury and are therefore insufficient to state a claim under section 1962(b).

2. Plaintiffs Fail to Plead that the Defendants "Operated or Managed" the Enterprises Under Section 1962(c)

To state a claim under RICO section 1962(c), a plaintiff must plead that the defendant conducted or participated in the affairs of an enterprise:

> It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

18 U.S.C. § 1962(c). In *Reves v. Ernst & Young*, 507 U.S. 170 (1993), the Supreme Court held that to conduct or participate in an enterprise's affairs, "one must participate in the operation or management of the enterprise itself." *Id*. at 185. The Supreme Court ruled that this "operation and management" requirement is not satisfied by mere involvement in or assistance to the enterprise, but rather, requires actual direction and control of the enterprise's affairs. *See id.* at 177-79.

The operation or management test "is difficult to satisfy, and claims are often dismissed for failure to meet the Second Circuit's 'stringent standards.'" *Bank*, 2000 WL 1692844, at *5 n.6 (citations omitted). As such, courts in the Second Circuit repeatedly

have held that certain types of conduct are insufficient – as a matter of law – to state a RICO claim under *Reves*:

- **Providing goods or services essential to the enterprise**. A defendant does not operate or manage an enterprise simply by supplying goods or services essential to the enterprise. *See, e.g., Azrielli v. Cohen Law Offices*, 21 F.3d 512, 521-22 (2d Cir. 1994); *Brooklyn Law Sch.*, 2000 WL 1692844, at *5; *Department of Econ. Dev. v. Arthur Andersen & Co.*, 924 F. Supp. 449, 467 (S.D.N.Y. 1996); *Biofeedtrac, Inc. v. Kolinor Optical Enters. & Consultants, S.R.L.*, 832 F. Supp. 585, 591 (E.D.N.Y. 1993); *University of Md. v. Peat, Marwick, Main & Co.*, 996 F.2d 1534, 1539 (3d Cir. 1993).

- **Aiding and abetting the enterprise.** A defendant does not operate or manage an enterprise even when it knowingly aids and abets the illegal conduct of the enterprise. *See LaSalle Nat'l Bank v. Duff & Phelps Credit Rating Co.*, 951 F. Supp. 1071, 1090 (S.D.N.Y. 1996); *Schmidt*, 16 F. Supp. 2d at 346.

- **Concealing the enterprise's illegal activities.** A defendant does not operate or manage an enterprise even when it knowingly conceals an enterprise's illegal activities. *Department of Econ. Dev.*, 924 F. Supp. at 466-67; *Schmidt*, 16 F. Supp. 2d at 347.

In *Schmidt v. Fleet Bank*, for instance, the plaintiffs alleged that the defendant banks had operated and managed an enterprise that was engaged in a fraudulent investment scheme. The banks provided the enterprise access to certain accounts, misrepresented to investors the status of their accounts, failed to notify authorities of irregularities in the banks' accounts, and helped the enterprise "to conceal the scheme generally." *Schmidt*, 16 F. Supp. 2d at 347. Although concluding that the defendants' alleged wrongful acts were of "real importance" to the scheme, the court nevertheless determined that "when reduced to their essentials, these are really allegations of assistance to the alleged RICO enterprise, not direction of it." *Id.*

Here, the essence of plaintiffs' claims is that defendants sold cigarettes to distributors whom they knew or should have known were involved in smuggling (or in selling to smugglers). (Colom. 2d Am. Compl. ¶¶ 32(a), (b); 33; 37(h)-(k), (r)-(t), (bb)-(hh) (PM); 38(a), (g), (u), (v), (aa) (BAT Defendants); EC Compl. ¶¶ 27(a), (b); 28; 32(c), (e)-(n), (t) (RJR); 33(a), (f)-(k), (m)-(n), (u) (PM).) That is not sufficient to state a claim of operation and management of an enterprise under the Second Circuit test. *See, e.g.*, *Department of Econ.*, 924 F. Supp. at 467. Applying these principles, the court in the *Amsterdam* case held that knowingly selling goods to smugglers is insufficient as a matter of law to fulfill the Second Circuit's stringent interpretation of the operation and management test. *See Amsterdam*, 107 F. Supp. 2d at 213-16. This result is consistent with the Second Circuit's long-held rule that a person does not violate the law merely by selling legal goods to a buyer whom the seller believes intends to use the goods to commit a crime. *See United States v. Falcone*, 109 F.2d 579, 581 (2d Cir.) (L. Hand, J.), *aff'd*, 311 U.S. 205 (1940).

Plaintiffs further allege that defendants hampered government efforts to police smuggling, encouraged smuggling by marketing lawfully imported cigarettes, and hid smuggling proceeds. These are no more than claims of assistance to – or aiding and abetting of – the alleged enterprise, not direction of it. *See Amsterdam*, 107 F. Supp. 2d at 217; *Schmidt*, 16 F. Supp. 2d at 347; *Biofeedtrac*, 832 F. Supp. at 591-92.

Finally, other than conclusory allegations of operation or management, which the Court properly may ignore,[25] the only remaining averment of direction of the enterprise is

[25] *First Nationwide Bank v. Gelt Funding Corp.*, 27 F.3d 763, 771-72 (2d Cir. 1994) (conclusory allegations regarding elements of RICO enterprise need not be accepted).

that defendants influenced the smugglers by cutting off cigarette sales for failure to abide by defendants' desired prices or other directives. (Colom. 2d Am. Compl. ¶ 37(j); EC Compl. ¶¶ 32(n), 33(i).) Again, however, this does not constitute operation or management. Someone who merely enjoys "substantial persuasive power to induce management to take certain actions . . . does not exercise control over the enterprise within the meaning of *Reves*." *Department of Econ. Dev*., 924 F. Supp. at 467 (citations omitted); *LaSalle*, 951 F. Supp. at 1090.

In sum, "[a]s interpreted by courts in this district and others, the 'operation and management' test set forth by the Supreme Court in *Reves* is a very difficult test to satisfy." *LaSalle*, 951 F. Supp. at 1090; *Schmidt*, 16 F. Supp. 2d at 346 (quoting same). Plaintiffs have not satisfied it here.

3. Because Plaintiffs' Fail to State A Claim Under RICO Sections 1962(a), (b), and (c), Their Conspiracy Claims Under Section 1962(d) Also Must Be Dismissed

The Colombian and EC Actions each allege a RICO conspiracy under section 1962(d). As the Second Circuit has recognized, however, "[a]ny claim under § 1962(d) based on conspiracy to violate the other subsections of section 1962 necessarily must fail if the substantive claims are themselves deficient." *Discon*, 93 F.3d at 1064 (internal citations omitted). The Supreme Court recently echoed this principle when it held that an "injury caused by an overt act that is not an act of racketeering or otherwise wrongful under RICO [] is not sufficient to give rise to a cause of action under 1964(c) for a violation of § 1962(d)." *Beck*, 529 U.S. at 505. As established above, all of the

Departments' and EC's claims under RICO sections 1962(a) through (c) fail to state a claim. Consequently, their conspiracy claims likewise fail.

V. ONLY THE UNITED STATES IS ENTITLED TO SEEK INJUNCTIVE OR EQUITABLE RELIEF UNDER RICO

Plaintiffs seek equitable relief (Colom. 2d Am. Compl. ¶ 46; EC Compl. ¶ 40) that is not available to them under RICO in any form. Although RICO allows the U.S. government to obtain equitable relief, the only provision that creates a remedy for private RICO plaintiffs is section 1964(c), which explicitly limits the relief to actual monetary damages. *See* 18 U.S.C. § 1964(a), (c).

Numerous courts have held that private plaintiffs may not obtain injunctive relief under RICO. *See Religious Tech. Ctr. v. Wollersheim*, 796 F.2d 1076, 1077 (9th Cir. 1986) ("injunctive relief is not available to a private plaintiff in a civil RICO action"); *Kaushal v. State Bank of India*, 556 F. Supp. 576, 582-84 (N.D. Ill. 1983) (private plaintiff seeking injunctive relief is entitled only to monetary damages under section 1964(c)); *Town of West Hartford v. Operation Rescue*, 726 F. Supp. 371, 377-78 (D. Conn. 1989) (same), *rev'd on other grounds*, 915 F.2d 92 (2d Cir. 1990); *Oregon Laborers-Employers Health & Welfare Trust Fund v. Philip Morris Inc.*, 185 F.3d 957, 967-68 (9th Cir. 1999) (same); *Curley v. Cumberland Farms Dairy, Inc.*, 728 F. Supp. 1123, 1137-38 (D.N.J. 1990) (same); *Vietnam Veterans of America, Inc. v. Guerdon Indus., Inc.*, 644 F. Supp. 951, 960-61 (D. Del. 1986) (same).

Although the Second Circuit has not yet explicitly addressed the issue, it has expressed "serious doubts" about injunctive relief for private RICO plaintiffs, *Trane Co. v. O'Connor Sec.*, 718 F.2d 26, 28 (2d Cir. 1983), and suggested in *Sedima v. Imrex Co.*,

Inc., 741 F.2d 482, 490-91 (2d Cir. 1984), *rev'd on other grounds*, 473 U.S. 479 (1985), that such relief would not be available. Moreover, this Court has held that "Congress did not empower the district courts to grant provisional relief in the form of preliminary injunction to private plaintiffs in civil RICO cases." *Bernard v. Taub*, No. 90 Civ. 0501(ADS), 1990 WL 34680, at *3 (E.D.N.Y. Mar. 21, 1990).

Other courts have concluded that RICO bars all forms of equitable relief sought by private litigants. *See, e.g., Ashland Oil, Inc. v. Gleave*, 540 F. Supp. 81, 84-86 (W.D.N.Y. 1982) (court could not order attachment under civil RICO); *City of Chicago Heights v. Lobue*, 914 F. Supp. 279, 283-84 (N.D. Ill. 1996) (plaintiff could not obtain disgorgement of profits because equitable remedies are unavailable under civil RICO); *Miller v. Affiliated Fin. Corp.*, 600 F. Supp. 987, 994 (N.D. Ill. 1984) (striking plaintiff's claims for declaratory judgment, order compelling return of property and injunction because such equitable remedies are not available under civil RICO); *Volckmann v. Edwards*, 642 F. Supp. 109, 115-16 (N.D. Cal. 1986) (denying plaintiff's request for rescission because private RICO plaintiffs are not entitled to equitable relief); *Potomac Elec. Power Co. v. Electric Motor & Supply, Inc.*, 119 F. Supp. 2d 546, 551 (D. Md. 2000) (recission is unavailable because private RICO plaintiffs are not entitled to equitable remedies); *Kaushal*, 556 F. Supp. at 584 (the same reasoning that required denial of injunctive relief would apply to all equitable relief requested by private RICO plaintiffs); *see also Johnson v. Collins Entm't Co.*, 199 F.3d 710, 726 (4th Cir. 1999) ("[t]here is substantial doubt whether RICO grants private parties . . . a cause of action for equitable relief . . . . This doubt is especially acute in light of the fact that Congress has declined to authorize injunctive remedies for private parties.") (citations omitted).

In deciding that equitable relief is not available to private RICO plaintiffs, courts have relied on standard principles of statutory interpretation. "[T]he inclusion of a single statutory reference to private plaintiffs, and the identification of a damages and fees remedy for such plaintiffs in part (c), logically carries the negative implication that no other remedy was intended to be conferred on private plaintiffs." *Wollersheim*, 796 F.2d at 1083; *see also Kaushal*, 556 F. Supp. at 582 (same); *Curley*, 728 F. Supp. at 1137 ("that Congress made an express provision for an equitable remedy in suits brought by the government and simultaneously declined to make a similar provision for private actions carries with it the strong suggestion that no private equitable remedy was intended."). Courts have cited Supreme Court precedent noting: "[I]t is an elemental canon of statutory construction that where a statute expressly provides a particular remedy or remedies, a court must be chary of reading others into it." *Wollersheim*, 796 F.2d at 1088 (citing *Transamerica Mortgage Advisors, Inc. v. Lewis*, 444 U.S. 11, 19 (1979)); *see also Kaushal*, 556 F. Supp. at 584 ("a court may read additional judicial remedies into 'elaborate [statutory] enforcement provisions' only where 'strong indicia of a contrary congressional intent' negate the implication 'Congress provided precisely the remedies it considered appropriate'" and "there are no 'strong indicia' . . . of Congress' intent to infer private equitable remedies under RICO.") (quotation source omitted); *Vietnam Veterans of America*, 644 F. Supp. at 961 ("Clearly, where Congress has provided for a particular remedy, and specifically rejected another remedy, the court should not create an implied right of action to the very remedy that Congress rejected.").

RICO's legislative history bears out these cases. Initial drafts of RICO contained no private right of action whatsoever and the private treble damages provision was added

only late in the legislative process. *See Kaushal*, 556 F. Supp. at 583 (citing S. Rep. No. 617, 91st Cong. 1st Sess. 24, 34, 80-83, 160 (1969)). "Thus the private damages remedy was engrafted onto a statutory scheme that had been complete on its own terms (with Section 1964(a) conferring jurisdiction and Section 1964(b) defining who could invoke it)." *Id.* Two inferences can, therefore, be drawn: (1) "Section 1964(c) is quite independent of Section 1964(a)"; and (2) "Section 1964(a)'s provisions spell out the governmental equitable remedies available under Section 1964(b), not the private remedy available under Section 1964(c)." *Id.*

In addition, Congress rejected early versions of the proposed RICO statute, such as bill H.R. 19215, which provided equitable relief for private parties under section 1964(a), and instead adopted H.R. 19586, which includes the provision that became section 1964(c). *Wollersheim*, 796 F.2d at 1083-85. Therefore, courts have reasoned that "[i]n choosing H.R. 19586 over H.R. 19215, the House apparently explicitly rejected a private injunctive relief provision." *Wollersheim*, 796 F.2d at 1085; *see also Curley*, 728 F. Supp. at 1137 (because Congress rejected versions of the RICO legislation that included a private equitable remedy, "Congress apparently explicitly rejected a private injunctive relief provision.") (citations omitted).

Congress also repeatedly failed to enact amendments that would have authorized private equitable remedies under section 1964(a). *Wollersheim*, 796 F.2d at 1085-86; *see also Vietnam Veterans of America*, 644 F. Supp. at 960-61 (relying on Congress' rejection of "attempts to amend RICO to provide private injunctive remedies" in holding that such remedies are not available). Taking all the legislative history into account, the "clear message . . . is that, in considering civil RICO, Congress was repeatedly presented

with the opportunity expressly to include a provision permitting private plaintiffs to secure injunctive relief. On each occasion, Congress rejected the addition of any such provision." *Wollersheim*, 796 F.2d at 1086. Because the plain language of the statute makes clear that private RICO plaintiffs are entitled only to monetary damages and because the legislative history demonstrates that Congress did not intend to provide private equitable remedies, plaintiffs' requests for injunctive relief here should be dismissed.

VI. PLAINTIFFS FAIL TO PLEAD WITH SUFFICIENT SPECIFICITY AS REQUIRED BY FEDERAL RULE OF CIVIL PROCEDURE 9(B)

A. Plaintiffs Fail to Connect Particular Fraudulent Acts to Specific Defendants

Federal Rule of Civil Procedure 9(b), which applies to RICO complaints, requires plaintiffs to "connect the allegations of fraud to each individual defendant . . . . [T]he complaint cannot generally refer to fraudulent acts by all or some of the defendants because each defendant is entitled to be informed of facts surrounding the allegations so that they may respond." *Colony at Holbrook, Inc. v. Strata G.C. Inc.*, 928 F. Supp. 1224, 1231 (E.D.N.Y. 1996) (citations omitted); *accord Amalgamated Bank of New York v. Marsh*, 823 F. Supp. 209, 216 (S.D.N.Y. 1993) ("Where there are multiple defendants, the complaint must disclose the specific nature of each defendant's participation in the alleged fraud."); *Sears v. Likens*, 912 F.2d 889, 893 (7th Cir. 1990) (Rule 9(b) is not satisfied if complaint groups defendants together without specifying which defendant was involved in which fraudulent activity).

Plaintiffs here make no effort to distinguish among the particular defendants or to identify which corporate defendant allegedly made which purportedly false statements.

Rather, the Complaints improperly group defendants and attribute conduct only to the amorphous "Philip Morris Defendants," "BAT Defendants," or "RJR Defendants." (Colom. 2d Am. Compl. ¶¶ 11 ("the foregoing Philip Morris-related entities are collectively referred to herein as the 'Philip Morris Defendants.'"); 21 (same for BAT Defendants); EC Compl. ¶¶ 20 (PM); 12 (RJR).) That alone is grounds for dismissal under Rule 9(b). *See, e.g.*, *Mills v. Polar Molecular Corp*., 12 F.3d 1170, 1175 (2d Cir. 1993) ("Rule 9(b) is not satisfied where the complaint vaguely attributes the alleged fraudulent statements to 'defendants.'"); *Colony at Holbrook*, 928 F. Supp. at 1232 (dismissing complaint under Rule 9(b) where the complaint "contains sweeping and general allegations of mail and wire fraud directed at all the defendants rather than connecting the alleged fraud to the individual defendants.").

B. Plaintiffs Fail Sufficiently to Allege Claims Against the Defendant Holding Companies

Recognizing that defendant Philip Morris Companies Inc. ("PMC") is a mere holding company for some of the remaining Philip Morris defendants and that R.J. Reynolds Tobacco Holdings, Inc. ("R.J.R. Holdings") is merely a holding company for all of the remaining R.J. Reynolds defendants (Colom. 2d Am. Compl. ¶¶ 7-11 (PMC); EC Compl. ¶¶ 17-20 (PMC); EC Compl. ¶¶ 7-12 (R.J.R. Holdings)), plaintiffs do not allege any specific or direct involvement by PMC or R.J.R. Holdings in the purported smuggling schemes, but instead simply group all of Philip Morris-related and R.J. Reynolds-related defendants together and make allegations against the "Philip Morris Defendants" and the "R.J. Reynolds Defendants." Plaintiffs apparently seek to hold PMC and R.J.R. Holdings liable for the alleged conduct of PMC's and R.J.R. Holdings'

operating subsidiaries under a "piercing the corporate veil" theory by alleging that these holding companies have "a 'worldwide' policy that purports to exercise control of the activities of its employees, as well as those of its direct and indirect subsidiaries." (Colom. 2d Am. Compl. ¶ 13; EC Compl. ¶¶ 17, 12.) Plaintiffs' veil piercing theory fails as a matter of law.

"It is a general principle of corporate law deeply 'ingrained in our economic and legal systems' that a parent corporation (so-called because of control through ownership of another corporation's stock) is not liable for the acts of its subsidiaries." *United States v. Best Foods*, 524 U.S. 51, 61 (1998) (citation omitted); *accord De Jesus v. Sears, Roebuck & Co.*, 87 F.3d 65, 69-70 (2d Cir. 1996). The doctrine of piercing the corporate veil is an infrequently imposed limitation on this general rule. *See Sears Roebuck*, 87 F.3d at 70. To survive a motion to dismiss a claim based on a veil piercing theory, a plaintiff may not rely on conclusory statements, but must plead with specificity facts demonstrating that:

> (1) the parent exercised complete domination over the subsidiary such that "the subsidiary has no separate will of its own"; and
>
> (2) "such domination must have been used to commit fraud or wrong against plaintiff, which proximately cause plaintiff's injury."

American Protein Corp. v. AB Volvo, 844 F.2d 56, 60 (2d Cir. 1988)*; see also Campo v. First Nationwide Bank*, 857 F. Supp. 264, 270-71 (E.D.N.Y. 1994). A failure to meet these stringent pleading requirements mandates dismissal.

In *Sears Roebuck*, for example, the Second Circuit dismissed RICO claims against a parent corporation where the plaintiff failed to allege specifically how the

parent exercised control over and used its subsidiaries to commit the alleged misconduct, but instead simply made conclusory allegations regarding domination and control. *See Sears Roebuck*, 87 F.3d at 70 (allegations that parent "determined the business objectives and goals of" the subsidiary and that the subsidiary's actions were "caused by, known to, and ratified by" parent held insufficient to state a claim). Indeed, in other contexts, New York state courts repeatedly have recognized that PMC is a mere "holding company which does not design, manufacture or sell cigarettes" and have dismissed plaintiffs' futile attempts to show that PMC and other holding companies control their subsidiaries. *See, e.g.*, *Cresser v. American Tobacco Co*., 662 N.Y.S.2d 374 (N.Y. Sup. Ct. 1997); *Biasucci v. Philip Morris Inc.*, No. 11402/97 (N.Y. Sup. Ct. 1997); *Cohen v. Philip Morris Inc.*, No. 12351/97 (N.Y. Sup. Ct. 1997).

In *Cresser* (nine cases that were consolidated for motions practice), for instance, the court dismissed claims against PMC and RJR Nabisco, Inc.[26] because the plaintiffs failed specifically to allege how these holding companies dominated and controlled their subsidiaries:

> This insistence upon specificity in pleadings that seek to pierce the corporate veil can be understood in light of our courts' reluctance to disregard corporate form . . . and insistence upon a showing that 'the owners, through their domination, abused the privilege of doing business in the

[26] The Complaint names, among others, the following entities as defendants: RJR Nabisco, Inc. ("RJRN"); RJR Nabisco Holdings Corp. ("RJRN Holdings"); and Nabisco Group Holdings Corp. ("NGH"). As a result of a number of corporate transactions in 1999 and 2000, RJRN was renamed R.J. Reynolds Tobacco Holdings, Inc., RJRN Holdings was renamed NGH and NGH was subsequently renamed RJR Acquisition Corp. R.J. Reynolds Tobacco Holdings, Inc. (formerly named RJRN) is currently the parent of named defendants R.J. Reynolds Tobacco Company and R.J. Reynolds Tobacco International, Inc., and of R.J. Reynolds Acquisition Corp. (formerly named RJRN Holdings and NGH). RJR Holdings now stands in the shoes of R.J.R. Nabisco as the holding company. Therefore, the courts' reasoning regarding R.J.R. Nabisco is equally applicable to R.J.R. Holdings.

> corporate form to perpetrate a wrong or injustice against that party such that a court in equity will intervene'. . . The pleadings with regard to the corporate parents do not conform to these standards and consequently must be dismissed.

Id. at 378 (citations omitted). Likewise, in *Biasucci*, the court dismissed all claims against PMC because the complaint was "silent" regarding how PMC allegedly controlled one of its subsidiaries:

> At the pleading stage of the action, it is necessary for the complaint to allege the means by which the parent corporation controlled its wholly owned subsidiary with respect to the tortious conduct alleged . . . . In this case, other than the fact that PMI is a wholly owned subsidiary of PMC, the complaint is silent as to the means by which PMC allegedly controlled its subsidiary. This is insufficient.

Id. at 2 (citations omitted).

In the present cases, plaintiffs fail to allege *any* fact showing that PMC or R.J.R. Holdings exercised "complete domination" over their subsidiaries or used this alleged domination to facilitate the alleged smuggling scheme. Plaintiffs' only allegations of control are that PMC and R.J.R. Holdings own stock in their subsidiaries and that these holding companies issue "corporate directives" that their subsidiaries "work together" with regard to cigarette sales. (Colom. 2d Am. Compl. ¶ 12; EC Compl. ¶¶ 12, 20.) Mere stock ownership, however, is insufficient to support a veil piercing claim. *See Sears Roebuck*, 87 F.3d at 69 ("Ownership by a parent of all its subsidiary's stock has been held an insufficient reason in and of itself to disregard distinct corporate entities."). Moreover, plaintiffs' conclusory allegations regarding "corporate directives" fail to allege conduct outside the usual activities of a holding company and, in any event, fail to

specify any particular instance where the holding companies used the alleged dominance to commit the purported wrongdoing.

Accordingly, all claims against the holding companies, defendant Philip Morris Companies Inc., and defendant R.J. Reynolds Tobacco Holdings, Inc., should be dismissed as a matter of law.

VII. PLAINTIFFS' PENDENT STATE LAW CLAIMS SHOULD BE DISMISSED

Plaintiffs assert that the Court has supplemental jurisdiction and diversity jurisdiction over their state law claims. (Colom. 2d Am. Compl. ¶ 26; EC Compl. ¶ 21.) Curiously, they also allege subject matter jurisdiction under the "All Writs Act," 28 U.S.C. § 1651. All three attempts fail.

First, the Supreme Court has emphasized that "pendent jurisdiction is a doctrine of discretion, not of plaintiff's right." *United Mine Workers v. Gibbs*, 383 U.S. 715, 726 (1966). In accordance with that principle, the Second Circuit routinely recognizes that where all federal claims are dismissed before trial, interests of efficiency, fairness, and comity mandate that "the state claims should be dismissed as well." *See, e.g.*, *Castellano v. Board of Trustees of the Police Officers' Variable Supplements Fund*, 937 F.2d 752, 758 (2d Cir. 1991); *Gordon v. Griffith*, 88 F. Supp. 2d 38, 58 (E.D.N.Y. 2000). Since, plaintiffs' federal RICO claims should be dismissed, the pendent common law counts should be dismissed too.[27]

[27] This is particularly the case where, as here, the pendent claims themselves fail to state a claim. For example, like plaintiffs' RICO counts, all of plaintiffs' common law counts fail sufficiently to allege that defendants' conduct was the proximate cause of plaintiffs' alleged injuries or that defendants made (and plaintiffs relied upon) fraudulent representations. *See Bennett v. United States Trust Co. of New York*, 770 F.2d 308, 315-16 (2d Cir. 1985) (dismissing common law counts on same causation grounds as federal counts); *Laborers Local*, 191 F.3d at 242 (dismissing fraud and special duty causes of action on same

(footnote continued on next page)

Second, there is no diversity jurisdiction over plaintiffs' state law claims because complete diversity is lacking. The Second Circuit has long recognized the "explicit and unequivocal" rule requiring complete diversity, and dismisses actions when aliens are on both sides of a matter. *See, e.g., Corporacion Venezolana de Fomento v. Vintero Sales Corp*., 629 F.2d 786, 790 (2d Cir. 1980) ("[T]he presence of aliens on two sides of a case destroys diversity jurisdiction."); *accord Franceskin v. Credit Suisse*, 214 F.3d 253, 258 (2d Cir. 2000) (following *Corporacion Venezolana*); *International Shipping Co. v. Hydra Offshore, Inc.*, 875 F.2d 388, 391 (2d Cir. 1989) (same). In both the Colombian and EC Actions there are aliens on both sides. (Colom. 2d Am. Compl. ¶¶ 16, 17, 21; EC Compl. ¶ 14.) That destroys diversity jurisdiction.

Third, the All Writs Act does not confer an independent basis of jurisdiction. *See Clinton v. Goldsmith*, 526 U.S. 529, 534-35 (1999) ("[T]he express terms of the [All Writs] Act confine the power of the [court] to issuing process 'in aid of' its existing statutory jurisdiction; the Act does not enlarge that jurisdiction."); *Collins v. United States*, No. 99 Civ. 6717, 2000 WL 516892, at *5 (E.D.N.Y. Mar. 8, 2000) (The All Writs Act "does not confer independent jurisdiction on a federal court. It only 'supplements the express powers of a court in cases in which jurisdiction already exists.'"). Here, there is no jurisdiction to supplement under the All Writs Act. Thus, there is no basis for jurisdiction over plaintiffs' state law claims.

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causation grounds as RICO counts); *Marcus v. AT&T Corp*., 138 F.3d 46, 63-64 (2d Cir. 1998) (dismissing pendent claims for fraud, negligent misrepresentation and unjust enrichment).

CONCLUSION

For the reasons set forth above, the Departments' Second Amended Complaint in case numbers 2881, 3857, and 4530, and the EC Complaint in case number 6617 should be dismissed in their entirety for failure to state a claim upon which relief can be granted.

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Respectfully submitted,

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